101-13

CURRENT CONDITION OF EASTERN AIR LINES AND THE PROSPECTS OF ITS RESTORATION AS A MAJOR CARRIER

(101-13)

HEARING

BEFORE THE

SUBCOMMITTEE ON AVIATION

OF THE

COMMITTEE ON
PUBLIC WORKS AND TRANSPORTATION
HOUSE OF REPRESENTATIVES

ONE HUNDRED FIRST CONGRESS

FIRST SESSION

JUNE 29, 1989

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SUBCOMMITTEE ON AVIATION

HEARING ON

THE CURRENT CONDITION OF EASTERN AIRLINES AND THE PROSPECTS FOR ITS RESTORATION AS A MAJOR CARRIER

THURSDAY, JUNE 29, 1989
2167 RAYBURN HOUSE OFFICE BUILDING

SUMMARY OF SUBJECT MATTER

At this hearing the Subcommittee will consider the current condition of Eastern Airlines and the prospects for its restoration as a major carrrier. The hearing notice set forth the following issues as being of particular interest to the Committee.

1) What has been the effect on consumers of the virtual shut down of Eastern? How have service and fares in the markets previously served by Eastern been effected?

2) What are Eastern's plans for expanding service in the next few months. Does it have the personnel and resources to carry out its plans and provide safe air transportation?

3) Does the bankruptcy court have jurisdiction to consider the public interest as well as the interests of Eastern's creditors? In evaluating proposals to reorganize (including proposals to sell Eastern to new owners) what weight can the bankruptcy court give to whether a plan would further the public interest in increasing competition in the airline industry, to the effects of a plan on Eastern's employees and the communities in which these employees are based, and to the effects on the communities served by Eastern?

4) Has the Department of Transportation taken any steps to consider the effects of various proposals for reorganization on Eastern's employees, on the communities it serves and on the traveling public? Has the Department taken any steps to urge the bankruptcy court to consider these matters?

5) What proposals have been presented for Eastern's reorganization? What is the likelihood that each proposal will permit Eastern to restore its operations to the level of a major carrier? What is the probable effect of each proposal on the traveling public and Eastern's employees, as well as on Eastern's creditors?

Eastern's Current Status

Since early March, Eastern has been virtually shut down by a strike of the International Assocation of Machinists (representing Eastern's mechanics and ground service personnel), and the honoring of picket lines by other unionized employees. Eastern now operates less than 20% of its pre-strike service.

On March 9, Eastern filed for Chapter 11 bankruptcy in New York City. The bankruptcy proceedings are now in progress.

Previous Committee Action

On March 7, shortly after the Eastern strike began, the Committee held hearings on Eastern's labor-management dispute. Shortly thereafter the Committee reported and the House passed legislation (H.R. 1231, passed on March 15, 1989) to require the President to appoint an Emergency Board to make recommendations for the resolution of the Eastern labor-management dispute. Under the legislation, Eastern's employees would have been required to return to work under their last effective contracts while the Emergency Board was studying the problem.

The Senate has not taken any action on the legislation.

Overview of Bankruptcy Procedures

Eastern has filed under Chapter 11 of the Bankruptcy Code, which establishes procedures for development of a reorganization plan to permit the company in bankruptcy (the debtor) to settle with its creditors and if possible, to resume operations. While in bankruptcy the company is relieved of its obligation to pay prior debts, and its operations are supervised by the court.

Ordinarily, the company filing for bankruptcy (called the "debtor in possession") continues to manage the company under the Court's supervision. The regular procedure provides that the debtor in possession will file a reorganization plan within 120 days after the bankruptcy filing. During this period the debtor has the exclusive right to file a plan. The creditors vote on whether to accept the plan, and if a sufficient number of creditors vote to accept, the Court then decides whether to accept the plan. If the debtor's plan has not been accepted by the creditors within 180 days after the filing of the bankruptcy petition, other parties in interest may file their own plan.

Although these are the regular procedures, in reality an aggressive judge has considerable leverage (such as his power to appoint a trustee to manage the company) to force a reluctant debtor to accept a plan different from that proposed by the debtor.

The Eastern case is in the stage preceeding the filing of the initial reorganization plan by the debtor. Unless the date is extended, Eastern must file its plan by July 7.

Developments in Bankruptcy Proceeding

The presiding judge in the bankruptcy proceedings in Judge Burton Lifland who has handled a number of major bankruptcy cases including the reorganizations of the Manville Corp., Allis-Chalmers Corp., and LTV Corp.

The first major issue in Eastern's bankruptcy proceeding was whether Eastern's existing managment would continue to manage Eastern during the bankruptcy proceedings, or whether the judge would grant a request by Eastern's unions to appoint a trustee to run the company. In late March the Judge decided that for the present, existing managment would remain in control but the judge would appoint an examiner with broad powers. The examiner would not only review pre-petition sales of assets by Eastern to its parent company Texas Air, but would have broad powers to meditate "impediments to a plan of reorganization" including disputes between management and labor. "It's a way of banging heads together by an independent entity," Judge Lifland stated. (Wall Street Journal, March 24, 1989)

The Examiner appointed was Washington attorney David Shapiro, who has extensive experience in complex litigation including service as special master in the litigation over Agent Orange.

X

In April, there were negotiations over a plan to acquire Eastern by a group led by Peter Uberroth. The deal appeared to be ready to go forward, but fell through when Frank Lorenzo, Eastern's owner, Eastern's Unions, and Uberroth could not agree on whether Lorenzo would continue to run Eastern until the Uberroth deal was final. Basically, Lorenzo did not want to give up control of the company to a trustee while Uberroth had rights to back out of the deal, the unions did not want to return to work while Lorenzo was in control, and Uberroth was unwilling to give up his rights to walk away from the deal.

Following the failure of the Uberroth plan the judge and the examiner decided to follow a two track approach. Work would go forward on Eastern's plan to sell $1.8 billion in assets and resume operations as a smaller carrier. Secondly, there would be a search to find viable proposals by outsiders to purchase Eastern.

1. Eastern's Proposal

Since the failure of the Uberoth proposal, Eastern's position has been that it does not want to sell to outsiders and that it wants to sell assets and resume operations as a smaller carrier. Eastern has not filed a final detailed plan, but it has announced a general plan to: 1) Sell $1.8 billion of assets which would enable it to repay $914 million of debt. 2) Operate a down sized operation with 157 aircraft serving 77 cities. (This is 62% and 75% respectively of the pre-strike carrier). 3) Although specific operating plans have not been disclosed, Eastern plans to concentrate on service out of its Atlanta hub and to sell the routes and assets used to serve South America, the Carribean and Canada. Eastern forcasts that its reorganized operations would realize a net profit of $25 million in 1990, increasing to $237 million in 1993.

Examiner Shapiro has given some encouragement to Eastern's plan, saying that he thought it is credible if four assumptions could be met: "that there would be no rescession in the U.S. economy; that Eastern would meet its target of employing 1700 pilots; that 'there would be a large amount of cash available to Eastern that would be tightly controlled' for start up and operations; and that Texas Air 'would not seek to use any Eastern Air assets to solve its own problems'". (Wall Street Journal, June 2, 1989)

The Examiner's conclusions are strongly challenged by Eastern's unions and by the Ritchie Group which is seeking to buy Eastern with union support. These parties challenge Eastern's ability to hire and train the pilots that will be needed and to realize the revenues and cost reductions it forcasts. They predict that the plan will fail quickly and that Eastern will have to be liquidated.

Since the failure of the Uberoth plan the bankruptcy court has permitted Eastern to sell a number of its assets.

In May, the Bankruptcy Court approved the sale of Eastern's shuttle to Donald Trump for $365 million. The assets sold included 21 aircraft, and gates and slots in New York, Boston and Washington.

In June, the count approved a sale of $206 million in assets to Midway Airlines. The assets included 16 aircraft and 8 gates at Philadelphia. Originally, Eastern had proposed to sell the assets to U.S. Air, but the Departments of Transportation and Justice objected on anti-trust grounds.

On June 15, the bankruptcy court approved the sale of 15 aircraft to a leasing company for $277 million.

As a result of these asset sales, Eastern's pre-strike fleet of 255 aircraft has been reduced to about 200.

2. Proposals by Outside Groups

Although Eastern has indicated that it does not intend to sell to an outside group, the examiner has conducted a search for outside groups with viable offers. His view is that if Eastern refuses to accept a good offer the judge can take action to encourage or require acceptance. The examiner also believes that it is critical that proposals by outsiders include putting cash into the company. In his view, this will help persuade the creditors to support an offer in preference to liquidation of the company. The Examiner believes that the creditors need to have confidence that an outside investor will have his own money at risk and that he will share in the costs of starting up Eastern's operations.

Of the offers which surfaced and were investigated, there is only which appears to be currently active, a proposal put together by a group led by Joseph Ritchie a Chicago commodities trader. The examiner's treatment of the Ritchie Proposal is controversial.

On June 14, the examiner told the court that he did not regard the Richie proposal as viable for the following reasons:

> ". . . As of now there is no viable bid out there that has been made for the purchase of this airline as a going concern in the Examiner's opinion. And that's based on two separate considerations.

> One on the basis of a very careful examination by my expert * the proposal made by the Ritchie Group was defective operationally.
>
> Number two, contrary to my instructions to the Ritchie group for something like five weeks I asked them, I begged them to put at least $200 million in cash on the table of Mr. Lorenzo and maybe we will have something to work with.
>
> Only at the last moment was there . . . an approach to Texas Air in Texas, and even then there was no cash put on the table despite my entreaties"

---

*Harry Kimbriel, an expert jointly selected by the Airline Pilots and Eastern

From the examiner's standpoint, there were three conditions which had to be met by the Richie Group. Preliminary, they had to show the ability to raise $100 million in cash, to show that they were a serious bidder. Secondly, they had to develop a sound plan for operating the airline and also a sound financial plan for the airline. The Examiner wanted the financial plan to be comparable to the Uberroth offer which involved putting $200 million in cash into the company. The Examiner's position was based on the fact that the company is now in worse financial shape than it was at the time of the Uberroth offer. If Lorenzo would be unwilling to accept a new offer of $200 million, which is the same as the Uberoth offer which had been acceptable to Lorenzo, then Lorenzo would be acting irrationally and further steps could be taken by the judge to encourage a sale.

The Ritchie Group feels that the examiner never indicated that they would have to put up more than $100 million. In their view, when they came up with the $100 million, the examiner upped the ante to $200 million. The Ritchie Group feels that $200 million is unreasonable because the company is now worth much less than when Uberroth made his offer.

The basis for the Examiner's conclusion that the Ritchie operational plan is unfeasible was the examiner's understanding that Ritchie contemplated retaining all of Eastern's employees and that it would not be operationally feasible for Eastern to return to a full-fledged pre-strike operation.

The Ritchie Group is expected to discuss its operating plan in detail at the hearing. It is our understanding that they propose a more extensive operation than the plan of Eastern's management. Ritchie contemplates operations with about 190 aircraft while Lorenzo contemplates operations with 157 aircraft. While Lorenzo proposes dropping Eastern's Miami hub, Ritchie would keep the Miami hub and keep Eastern's service to the Carribean and South America.

ORGANIZATION AND OWNERSHIP OF EASTERN

For the Committee's background, this section summarizes briefly the complex organizational structure of which Eastern is currently a part. Eastern's common stock is owned by the Texas Air Corporation, a holding company based in Houston, Texas. Texas Air also owns all of the common stock of Continental Airlines, System One Holdings Inc. (which owns a computer reservations system), and a number of other subsidiaries which hold assets and provide aeronautical services. Frank Lorenzo is the Chairman of Texas Air and is also Chairman of the Board of Eastern.

Texas Air in turn is controlled by Jet Capital Corp. which controls 35% of the voting stock of Texas Air. Jet Capital in turn is controlled by Frank Lorenzo.

SERVICE IN EASTERN'S MARKET SINCE THE STRIKE

The Department of Transportation will testify in detail as to how the strike has affected service in Eastern's major markets. The department has analyzed the top 45 markets served by Eastern before the strike, which accounted for 50% of Eastern's total passengers. Looking at these markets in the aggregate, DOT concluded that the departures offered in June 1989 (based on schedules shown in the Official Airline Guide) were substantially below the level of departures offered in June 1988. In June 1989, Eastern non-stop service in the 45 markets declined by 82%, while other carriers' service in these markets increased by 10%. The net result was a 22% decline in non-stop service in the 45 markets. For one-stop service, the decline in service in the 45 markets was 23%, and for multi-stop service the decline was 37%. The Department has advised us that they do not yet have any data which would permit them to analyze the impact which the strike has had on fares.

EXPECTED WITNESSES

Congressman Gingrich
Congressman John Lewis
Joseph Ritchie
Representatives of the Airlines Pilots Association
Representatives of the International Association of Machinists
Examiner David Shapiro
Eastern has been invited, but has not yet indicated whether it is willing to testify.

CURRENT CONDITION OF EASTERN AIR LINES AND THE PROSPECTS FOR ITS RESTORATION AS A MAJOR CARRIER

THURSDAY, JUNE 29, 1989

House of Representatives,
Subcommittee on Aviation,
Committee on Public Works and Transportation,
Washington, DC.

The subcommittee met, pursuant to notice, at 11:10 a.m., in room 2167, Rayburn House Office Building, Hon. James L. Oberstar, Chairman of the Subcommittee, presiding.

Mr. Oberstar. The subcommittee will come to order.

Today's hearings have been called to update the subcommittee on the current condition of Eastern Air Lines, and the prospects for its restoration as a major carrier.

There are substantial public policy concerns underlying the question of whether Eastern can emerge from bankruptcy as a major carrier. Eastern's demise would have serious effects on its owners, on its creditors, on its 30,000 employees, on the cities where those workers are based, and on the traveling public.

Eastern's total demise would mark a further serious decline in airline competition, and that would accelerate a trend which has concerned us very greatly.

In recent years, there has been a substantial loss of competition in the domestic air transportation industry. There have been 10 mergers of major airlines, along with the economic failure of most of the new entrants into the airline industry since deregulation.

The top eight airlines now carry more than 90 percent of total domestic traffic, and that is a substantial increase over the 74-percent share those carriers held in 1983.

The decreased competition may already be harming consumers. A recent study, still to be completed by the General Accounting Office, has shown that fares at hubs dominated by one or two carriers, the so-called "fortress hubs," are, on average, 27-percent higher than fares at comparable cities where there is more competition.

Before the strike, Eastern played a critical role in airline competition. It was the Nation's sixth-largest airline. It was a major carrier at many cities such as Atlanta, where it had 36 percent of the traffic.

In Miami it had 41 percent of the traffic, and in New York, Washington and Boston, it had about 20 percent of the traffic.

If Eastern is not able to resume operations, if its assets are liquidated, there is likely to be a substantial loss of competition which would deprive many passengers of the benefits for consumers of airline deregulation.

Every effort must be made to prevent that tragedy from occurring.

This Subcommittee on Aviation has taken steps to encourage the survival of Eastern. On March 7th, shortly after the employees of Eastern went on strike, we held hearings on the labor-management dispute. Shortly afterward, we reported, and the House passed, legislation to require the President to appoint an emergency board to make recommendations for the resolution of Eastern's labor-management problems.

Many of us in the House continue to feel, that had that legislation been enacted, the dispute would have been settled, the unions would have gone back to work, Eastern would have gone back to flying, and would have continued as a major competitor in the air-carrier industry.

Unfortunately, the Administration opposed the legislation. The Senate failed to take action. The strike continued, and, now, Eastern is in Chapter 11 bankruptcy proceedings.

The course of those proceedings has raised questions about whether it may lead to Eastern's survival, or to its dissolution.

Recently, the Bankruptcy Court indicated that it is unlikely to take action to encourage the sale of Eastern to new investors willing to make an effort to restore Eastern as a major competitor.

Instead, the Bankruptcy Court is proceeding with Eastern's own plan for reorganization which includes the sale of at least $1.8 billion in assets, and already, the Bankruptcy Court has approved the sale of substantial Eastern assets, including aircraft, gates, and slots.

As a result of these asset sales, Eastern's pre-strike fleet of 225 aircraft will be reduced to about 200 aircraft. Questions have been raised, whether these asset sales, and those that may come in the near future, will reduce Eastern below the critical mass needed for it to emerge as a major competitor.

In addition, there have been questions about whether Eastern's plan to resume operations as a down-sized carrier has any reasonable prospect of success, and how that plan compares with proposals of another group which will testify later this morning, headed by Mr. Ritchie, who proposes to restore most of Eastern's pre-strike operations.

Our hearings today are framed by a desire to inform the committee on the various proposals pendings, to inform the public on the course the bankruptcy proceeding to date, and we want to consider the role which the Department of Transportation is playing in the bankruptcy proceeding.

It is important for us to know whether the Department is keeping a close watch on those proceedings, and advising the parties, as well as the court, as to which proposals would further the broad public interest in Eastern, as well as serve the interests of Eastern's creditors.

I want to make it clear that we recognize the jurisdiction and the responsibilities of the Bankruptcy Court, these proceedings are only for the purpose of information, and for laying out issues in the public domain.

They are not designed to encourage the court to do anything other than carry out its responsibilities under the governing laws.

We, in the Congress, also have our responsibilities in this tripartite Government, and our responsibility is to protect the public interest in aviation through oversight, and, where appropriate, through legislation.

We have designed these hearings today to carry out those constitutional responsibilities. We have a very distinguished group of witnesses, I think a very long and perhaps complex presentation by many of them. I hope that members will enter their opening remarks in the record so that we may get on with the business of this hearing. I have simply tried to frame the issues in this opening statement, and at this point I recognize the gentleman from Pennsylvania. Mr. Clinger.

Mr. CLINGER. Thank you, Mr. Chairman. I would like to defer to the Ranking Member of the full committee, Mr. Hammerschmidt.

Mr. OBERSTAR. The Chair recognizes the gentleman from Arkansas, the Ranking Member of the full committee. Mr. Hammerschmidt.

Mr. HAMMERSCHMIDT. Thank you very much, Mr. Chairman, and thank you for holding these important hearings. I am going to comply with your admonishment of putting a statement in the record and I would ask permission to do that.

Let me say that I recognize the fact that this panel does not make decisions on private-sector airline transactions, but of course we do have a great interest in what national public policy is in the field of transportation. We are interested in all reasonable plans or ideas that might keep Eastern as a viable, competitive airline in our Nation's air transportation system. That is the reason we are here today.

Let me say, while I have the floor, that I am delighted with our first three witnesses, two members of this committee and one former member of the committee, I know we have a lot of important witnesses we are waiting to hear, so I will defer the rest of my statement. Thank you very much, Mr. Chairman.

[Mr. Hammerschmidt's prepared statement follows:]

STATEMENT OF HONORABLE JOHN PAUL HAMMERSCHMIDT FOR THE HEARING ON EASTERN AIRLINES

JUNE 29, 1989 11:00 A.M. 2167 RHOB

MR. CHAIRMAN:

THIS COMMITTEE HAS BEEN EMBROILED IN THE CONTROVERSY SURROUNDING EASTERN AIRLINES FOR SOME TIME NOW. LAST YEAR WE BACKED A HOUSE RESOLUTION CALLING FOR A INVESTIGATION OF TEXAS AIR AND EASTERN. EARLIER THIS YEAR, WE DEBATED LEGISLATION TO REQUIRE A PRESIDENTIAL EMERGENCY BOARD (PEB) TO INVESTIGATE THE DISPUTE BETWEEN EASTERN AND ITS UNIONS.

DESPITE OUR INVOLVEMENT, EVENTS AT EASTERN CONTINUE TO UNFOLD WITH TRAGIC CONSEQUENCES FOR MANY OF THE PEOPLE ASSOCIATED WITH THAT AIRLINE.

I THINK WE ALL AGREE THAT IT WOULD BE DESIRABLE FOR EASTERN TO SURVIVE AS A STRONG AND VIABLE COMPETITOR IN THE AIRLINE INDUSTRY. WHERE THERE MIGHT BE SOME DISAGREEMENT IS OVER THE MEANS TO ACHIEVE THAT END. I OPPOSED THE PEB, FOR EXAMPLE, BECAUSE I DID NOT BELIEVE THAT IT WAS JUSTIFIED UNDER THE LAW OR THAT IT WAS THE WAY TO RESOLVE THE DISPUTE BETWEEN MANAGEMENT AND LABOR AT EASTERN.

THE PROBLEM WE ARE FACING HERE IS NOT REALLY THE TRADITIONAL LABOR-MANAGEMENT DISPUTE OVER WAGES AND WORKING CONDITIONS. RATHER, IT IS A STRUGGLE OVER WHO SHOULD CONTROL THE AIRLINE. HOW THAT STRUGGLE IS RESOLVED WILL ULTIMATELY BE DECIDED BY THE BANKRUPTCY COURT AND BY THE PARTIES INVOLVED, NOT BY THE CONGRESS.

NEVERTHELESS, CONGRESS HAS AN IMPORTANT OVERSIGHT ROLE TO PLAY IN THIS PROCESS. WE, TOGETHER WITH DOT AND FAA, MUST ENSURE THAT AIRLINES ARE OPERATED SAFELY AND THAT THE AIRLINE INDUSTRY AS A WHOLE WILL REMAIN A COMPETITIVE BUSINESS. WE ARE INTERESTED IN ALL REASONABLE IDEAS THAT MIGHT SERVE TO KEEP EASTERN AS A VIABLE COMPETITIVE AIRLINE.

SO WHILE I WELCOME THIS HEARING, I WOULD BE CONCERNED IF WE WERE TO MOVE BEYOND THAT. HOWEVER, IT IS IMPORTANT THAT THIS SUBCOMMITTEE BE INFORMED OF DEVELOPMENTS IN THE EASTERN BANKRUPTCY CASE.

SO, WITH THAT, I WOULD LIKE TO JOIN YOU IN WELCOMING THE WITNESSES HERE TODAY AND LOOK FORWARD TO THEIR VERY IMPORTANT TESTIMONY.

Mr. **Oberstar**. I thank the gentleman. Does the gentleman from Pennsylvania have——

Mr. **Clinger**. Very briefly, Mr. Chairman. I ask that my entire statement be entered in the record.

Mr. **Oberstar**. Without objection, so ordered.

Mr. **Clinger**. I have a couple of comments.

This morning, we are going to be hearing from a number of the interested parties, including Eastern, regarding the airline's ability to reorganize itself and remain as a contender in the industry.

This hearing is not—as you have indicated, Mr. Chairman—to be a forum to promote any one particular reorganization plan. Rather, it is to give members of the committee a chance to question expert witnesses on their assessment of Eastern's future, either under present or different management, because we will also hear—as you have indicated—proposals to take control of Eastern through the bankruptcy proceedings.

As much as I am interested in the subject matter of the hearing, I do have reservations about its timing. I was reluctant to support a hearing that would occur prior to the court's July 7th deadline.

I was, and remain concerned, about the appearance of Congress unduly attempting to influence the court's decision. Obviously, though, there would be no point in discussing their reorganization plan after the court acts.

The question of alternative approaches to Eastern's future all but becomes moot. So with that thought in mind, I agreed to support today's hearing, not for the purpose of trying to influence the Bankruptcy Court, but solely to evaluate the prospects of Eastern remaining in business as a viable, competitive airline.

It is essential that Eastern continues to operate. There has been far too much consolidation in this industry, in my view, and I fear that in the next several years, too many communities will be solely relying on only one carrier for its service, and I think that is unhealthy for the industry and for the country.

Thank you, Mr. Chairman.

[Mr. Clinger's prepared statement follows:]

STATEMENT OF THE
HONORABLE WILLIAM F. CLINGER, JR.
BEFORE THE SUBCOMMITTEE ON AVIATION
DURING ITS HEARING ON
EASTERN AIRLINES
JUNE 29, 1989

Mr. Chairman, airlines are a major asset of our country. They provide an essential service; they do it efficiently, and the American citizen is clearly a beneficiary of this extraordinary industry. A growing segment of our nation's economy is now dependent on the success, frequency, and availability of a strong and competitive air service.

Eastern Airlines was once a dominant force in the industry, but in the years following deregulation, the company has faltered to the point that it has now sought protection by putting itself in bankruptcy.

I am deeply worried about the future of Eastern, for its employees and for the traveling public. We need to maintain a viable, competitive environment in the air transportation market in the U.S. and the collapse or dismemberment of Eastern would jeopardize ~~their~~ THIS objective.

This morning we'll be hearing from a number of interested parties, including Eastern, regarding Eastern's ability to reorganize itself and remain as a contender in the industry. This hearing is not to be a forum to promote any one particular reorganization plan; rather, it is to give Members of the Committee a chance to question expert witnesses on their assessment of

Eastern's future either under present or different management because we will also hear from an investor who wishes to take control of Eastern through the bankruptcy proceedings.

As much as I am interested in the subject, I do have reservations about the timing of this hearing. I was reluctant to support a hearing that would occur prior to the court's July 7 deadline. I was and remain concerned about the appearance of Congress unduly attempting to influence the court's decision.

Obviously, though, there would be no point in discussing their reorganization plan after the court acts. The question of alternative approaches to Eastern's future all but becomes moot. So with that thought in mind, I agreed to support today's hearing not for the purpose of trying to influence the bankruptcy court but solely to evaluate the prospects of Eastern remaining in business as a viable, competitve airline.

It is essential that Eastern continues to operate. There's been far too much consolidation in this industry, and I fear that in the next several years, too many communities will be solely reliant on only one carrier for its service -- and I think that is unhealthy.

Thank you, Mr. Chairman.

Mr. **Oberstar**. I thank the gentleman for those comments, and or his participation and cooperation in moving this hearing to the public.

The gentleman from Pennsylvania. Mr. Kolter.

Mr. **Kolter**. Thank you, Mr. Chairman. I, too, wish to commend you for calling today's hearings, and at your request, I will submit my remarks for the record.

[Mr. Kolter's prepared statement follows:]

Joe Kolter

MR. CHAIRMAN, I COMMEND YOU FOR CALLING TODAY'S HEARING TO LOOK INTO THE VIABILITY OF EASTERN AIRLINES. IT IS, I FEEL, IN THE BEST INTEREST OF ALL CONCERNED THAT THIS COMMITTEE INVESTIGATE THE CURRENT SITUATION AND RECOMMEND A REMEDY FOR EASTERN'S FUTURE.

ONCE THE BRIGHT STAR IN THE SKY OF DOMESTIC CARRIERS, EASTERN HAS BEEN DISMEMBERED AND CRIPPLED BY ITS PARENT COMPANY, TEXAS AIR. IT NOW SURVIVES AS A MERE SHADOW OF ITS FORMER SELF.

THE CHRONOLOGY OF EVENTS WHICH LED TO THE DEMISE OF THE AVIATION GIANT IS A SAD ONE. REFUSAL BY MANAGEMENT TO BARGAIN IN GOOD FAITH WITH ITS EMPLOYEES BROUGHT ON THE EVENTUAL COLLAPSE. YOU WILL REMEMBER THAT IT WAS EASTERN WHICH ASKED THE NATIONAL MEDIATION BOARD TO STEP IN TO RESOLVE THE IMPASSE BETWEEN MANAGEMENT AND LABOR. AFTER ATTEMPTS TO NEGOTIATE A SETTLEMENT, EASTERN, ON JANUARY 31st OF THIS YEAR, DECLINED THE BOARDS OFFER OF BINDING ARBITRATION. ON FEBRUARY 24th, THE BOARD RECOMMENDED THAT THE PRESIDENT APPOINT AN EMERGENCY PANEL TO MEDIATE THE IMPASSE, THIS, AS WE WELL KNOW, NEVER CAME TO PASS.

SINCE DEREGULATION OF THE AIRLINE INDUSTRY, WE HAVE SEEN A GRADUAL DECLINE IN THE NUMBER OF LARGE DOMESTIC CARRIERS. THE SIX LARGEST CARRIERS NOW CONTROL 77 PERCENT OF THE MARKET. IF WE WANT TO PROMOTE COMPETITION IN THE SKIES, IT IS IN OUR BEST INTEREST TO ENCOURAGE THE PROCESS OF EASTERN'S PURCHASE BY A WELL-INTENTIONED BUYER, ONE WHICH WILL BRING THE CARRIER BACK TO THE HEALTH THAT IT ONCE ENJOYED.

A PURCHASER MUST BE FOUND WHICH WILL OPERATE EASTERN'S EXTENSIVE FLIGHT ROUTES AND MAJOR AIRPORT HUBS. IT IS BECAUSE OF

THIS THAT I AM MOST EAGER TO HEAR THE INTENTIONS OF MR. JOSEPH RITCHIE IN HIS PROPOSAL TO PURCHASE EASTERN. FROM ALL INDICATIONS, IT SOUNDS LIKE THESE DESIGNS ARE INCLUDED IN MR. RITCHIE'S TAKEOVER PLAN.

I CANNOT STRESS TOO MUCH THE IMPORTANCE OF TODAY'S PROCEEDINGS TO AIRLINE WORKERS AND PASSENGERS. AN EQUITABLE RESOLUTION TO EASTERN'S TROUBLES MUST BE FOUND.

I THANK ALL OF THE WITNESSES FOR APPEARING BEFORE US TODAY. I LOOK FORWARD TO YOUR TESTIMONY.

THANK YOU, MR. CHAIRMAN.

Mr. **Oberstar**. I thank the gentleman for that. Mr. Molinari.

Mr. **Molinari**. I know you want to get started. Let me just say this. In reviewing the statements, and some of the testimony, I think the crux of what we are going to be hearing today revolves around a statement made by the examiner appointed by the Bankruptcy Court on June 14th relative to the offer made by Mr. Ritchie, and that statement is as follows.

> As of now, there is no viable bid out there that has been made for the purchase of this airline as a going concern. On the basis of a very careful examination by my expert, the proposal made by the Ritchie group was defective, operationally. In my view and in his view, the operational plan was not a viable one.

I would think that there is one thing we are going to do today, or we should do today, and that is to examine ourselves into the viability of the Ritchie offer, and whether it is operationally defective or not. Thank you, Mr. Chairman.

Mr. **Oberstar**. I thank the gentleman for his comments and getting to the heart of the matter.

Mr. Bosco.

Mr. Bosco. Mr. Chairman, I want to thank you for holding this hearing, and I, as the other members, will be anxious to see what role the Bankruptcy Court which now has jurisdiction over this matter is playing to ensure the public's interest, which I think predominates this entire matter.

Mr. **Oberstar**. I thank the gentleman. Mr. Inhofe.

[No response.]

Mr. **Oberstar**. Mr. Ballenger.

[No response.]

Mr. **Oberstar**. The gentleman from Tennessee.

[No response.]

Mr. **Oberstar**. The gentleman from Missouri.

[No response.]

Mr. **Oberstar**. Mr. Skaggs.

[No response.]

Mr. **Oberstar**. Mr. Payne.

Mr. **Payne**. Mr. Chairman, I want to commend you for holding this hearing and request permission to put an opening statement in the record.

Mr. **Oberstar**. Without objection, so ordered.

[Mr. Payne's prepared statement follows:]

LF Payne
JA-5

THE HONORABLE LEWIS F. PAYNE, JR.
SUBCOMMITTEE ON AVIATION
COMMITTEE ON PUBLIC WORKS AND TRANSPORTATION
June 29, 1989

MR. CHAIRMAN, thank you very much for your continued interest and leadership regarding the status of Eastern Airlines. I appreciate this opportunity today to review Eastern's present condition and possible alternatives to restore Eastern as a major carrier.

As Members of this Subcommittee, we are charged with the responsibility to examine all aspects of airline safety. I think it is very important that we continue in our efforts to ensure that the service Eastern provides is safe, and to a lesser note, does not pose a major inconvenience to the flying public. Rumors have abounded regarding the maintenance of Eastern's planes in light of the continuing strike by the machinists. Also, concerns exist regarding the future of Eastern airlines and its employees and the effect that a continued decrease in Eastern's assets will have on the industry.

Today's hearing is a great opportunity to review these concerns, as well as others, and I thank you again, Mr. Chairman, for providing this avenue to examine this matter further.

Mr. **Oberstar**. Before we proceed, I would like to insert into the record a statement from our colleague from Illinois, Representative Jerry Costello.

[Mr. Costello's statement follows:]

OPENING STATEMENT
BY U.S. REP. JERRY COSTELLO
COMMITTEE ON PUBLIC WORKS AND TRANSPORTATION
SUBCOMMITTEE ON AVIATION
JUNE 29, 1989
"THE STATUS OF EASTERN AIRLINES"

In recent months we have seen the devastating effect that the position of Eastern Airlines' management has taken on the lives of thousands of the airline's workers and their families. Because of Chairman Frank Lorenzo's refusal to engage in honest bargaining with the machinist's union, the union went on strike, and the workers' message has virtually been ignored since that time.

As a result, the workers have found that their once secure jobs are in extreme jeopardy. Eastern is on the brink of bankruptcy, and unless some kind of action is taken, we will see the end of the nation's sixth largest airline.

Where does the airline stand today? What efforts are being made to protect the workers, many of whom have been with Eastern for tens of years? How are consumers being accommodated as the airline is in this dormant period?

I am hopeful that today's hearing will answer many of these questions. It would be a pity to see corporate greed and mismanagement drive this once proud company into the ground. If there is any action that will save Eastern, I am hopeful today's hearing will help bring that solution to light.

Mr. OBERSTAR. At this time, the Chair recognizes the former Ranking Member of the Subcommittee on Aviation, our dear, departed colleague, departed from the subcommittee on a temporary basis while he serves in another capacity. The Honorable Republican Whip, Mr. Gingrich.

TESTIMONY OF HON. NEWT GINGRICH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF GEORGIA

Mr. GINGRICH. I very much thank my good friend, Mr. Oberstar, for holding this hearing, I thank you for allowing me to come here, and it is good to be back with you and John Paul Hammerschmidt, and Bill Clinger, and all my other friends.

It is a little bit eerie to be on this side of the table for the very first time and I appreciate the subcommittee's indulgence.

I think it is a matter of great concern to the members of this subcommittee, and to me, personally, to look at the Eastern situation.

Through Eastern's protracted period of mediation, followed by a crippling strike, and now Chapter 11 bankruptcy, my primary concern has been for the 31,000 families, including 7,000 in the Atlanta area, whose future is tied directly to that of Eastern Air Lines.

They are the major victims of the tragic events that have crippled this great airline. The current situation at Eastern raises a number of important questions and I commend the committee for holding this hearing in an effort to get some answers.

Obviously, I have a great deal of concern about what Frank Lorenzo actually has in mind for this troubled airline, now that he has placed it in bankruptcy.

In a fairly short period of time, Frank Lorenzo has given all of us an outstanding demonstration on how not to run an airline. His long and bitter battle with the unions has finally brought Eastern to Chapter 11 bankruptcy. Will he now sell off the airline piece by piece, or will he follow through on his stated intention to make Eastern profitable on a smaller scale?

The possibility exists that his true intention is not to operate a down-sized Eastern Air Lines at all, but to in fact liquidate Eastern and thereby eliminate a competitor of Continental Airlines.

Aside from the obvious impact on Eastern employees, liquidation would further increase concentration in the industry and create an even larger airline oligopoly than already exists.

This potential liquidation does not bode well for the deregulated marketplace. What we do know is that Frank Lorenzo has announced his intentions to sell off at least $1.8 billion of Eastern's assets.

Whether he will sell more is uncertain at this point. We have to wonder whether after this sell-off of assets Eastern can operate successfully, or whether this action signals the start of liquidation.

Some of these asset sales involve route rights which exist because they have been conferred by governmental action. Does Frank Lorenzo have the right to sell these rights, or is it in the public interest that the Government reclaim them, or, at a minimum, modify the terms of his ownership of them.

With these concerns in mind, this hearing should focus on whether the Department of Transportation should intervene at this point and contact the Bankruptcy Court to request a delay in the approval of further sales of Eastern assets, until it has had an opportunity to determine if the public interest is served by a downsized or non-existent Eastern Air Lines.

And here I would reemphasize something that Mr. Clinger said. That while, on the one hand, we do not want to get engaged in the details of a bankruptcy proceeding, on the other hand, it is terrible public policy to suggest that after everything has been done and after we determine that a major mistake has been made, then we will set policy for the next time this happens.

If there is a serious concern, for example, about routes sales as conferred by the Government, now is the time for the Department of Transportation to be involved.

So far, the Bankruptcy Court is permitting Frank Lorenzo to sell off assets and is not entertaining any new offers for investors interested in purchasing Eastern.

However, I think it is worth noting that an offer made by Joe Ritchie, head of the Options Trading Company, Chicago Research and Trading Group, might be a viable alternative to what Frank Lorenzo says that he will be doing.

The Ritchie proposal, as I understand it, would provide for employee ownership of part of the airline. That certainly would have appeal for Eastern's employees who, after all, want to save the airline, not kill it.

Yet as important as a healthy and competitive Eastern Air Lines is to its employees, this Nation and the flying public also have a major interest in this matter.

It serves the interest of no one to lose Eastern's competitive air service and to decrease competition in the airline industry.

In today's concentrated industry environment, eight carriers account for 90 percent of the traffic. We know, as well, that fares at highly concentrated airport hubs are much higher than at more competitive hubs.

Were Eastern to drop completely out of the picture, the situation would only worsen. Certainly Eastern's competitors have not been idle during all of this. Indications are that they have been able to accommodate Eastern's passengers with moderate increases in nonstop and one-stop flights, and possibly some increase in load factor in existing flights.

Transportation Secretary Samuel Skinner has expressed great concern over maintaining competition within the U.S. airline industry, so it is appropriate that during this hearing we consider whether the Department of Transportation and the Department of Justice should intervene in this matter to make certain that the public interest is protected.

These agencies, as well as the Congress, need time to consider the grave public concerns raised by Eastern's bankruptcy. We should consider today's hearing the first, not the last step in our deliberations on this matter.

I think that all of us would agree that the public interest would best be served by the operation of Eastern Airlines at full capacity and fully competitive in today's deregulated environment.

Certainly the employee work force exists to make that possible and the experience base of the Eastern employees would return them to competition in very short order.

Let me say, in closing—and I think both of my colleagues from Georgia who are going to speak would agree with this—that the most distressing thing is to recognize that this is not, in the abstract, simply an argument between unions and management; it is not simply, in the abstract, some argument between lawyers and a Bankruptcy Court; that there are literally thousands of families caught up, in terms of their health insurance, their pension plan, their hopes for their children to go to school, their chance of keeping the home they are trying to buy.

That at a very human level, we have now been into a 4-month endurance contest, and that in some significant ways there are both human concerns and national policy concerns that this committee is looking at today, and I again thank the Chairman and the Ranking Member for calling this hearing.

[Mr. Gingrich's prepared statement follows:]

STATEMENT OF THE HONORABLE NEWT GINGRICH
BEFORE THE SUBCOMMITTEE ON AVIATION OF THE
PUBLIC WORKS AND TRANSPORTATION COMMITTEE
JUNE 29, 1989

THANK YOU, MR. CHAIRMAN, FOR THIS OPPORTUNITY TO JOIN YOU AND MY VERY ABLE SUCCESSOR AS THE SUBCOMMITTEE'S RANKING REPUBLICAN MEMBER, CONGRESSMAN BILL CLINGER, AND MY OTHER FRIENDS AND COLLEAGUES ON THE SUBCOMMITTEE, AS YOU REVISIT THE SITUATION AT EASTERN AIR LINES.

THIS IS A MATTER OF GREAT CONCERN TO THE MEMBERS OF THIS SUBCOMMITTEE AND TO ME PERSONALLY. THROUGHOUT EASTERN'S PROTRACTED PERIOD OF MEDIATION, FOLLOWED BY A CRIPPLING STRIKE, AND NOW CHAPTER 11 BANKRUPTCY, MY PRIMARY CONCERN HAS BEEN FOR THE 31,000 FAMILIES, INCLUDING 7,000 IN THE ATLANTA AREA, WHOSE FUTURE IS TIED DIRECTLY TO THAT OF EASTERN AIR LINES.

THEY ARE THE MAJOR VICTIMS OF THE TRAGIC EVENTS THAT HAVE CRIPPLED THIS GREAT AIRLINE.

THE CURRENT SITUATION AT EASTERN RAISES A NUMBER OF IMPORTANT QUESTIONS, AND I COMMEND THE COMMITTEE FOR HOLDING THIS HEARING IN AN EFFORT TO GET SOME ANSWERS.

OBVIOUSLY, I HAVE A GREAT DEAL OF CONCERN ABOUT WHAT FRANK LORENZO REALLY HAS IN MIND FOR THIS TROUBLED AIRLINE, NOW THAT HE HAS PLACED IT IN BANKRUPTCY. IN A FAIRLY SHORT PERIOD OF TIME, FRANK LORENZO HAS GIVEN ALL OF US AN OUTSTANDING DEMONSTRATION ON HOW NOT TO RUN AN AIRLINE. HIS LONG AND BITTER BATTLE WITH THE UNIONS HAS FINALLY BROUGHT EASTERN TO CHAPTER 11 BANKRUPTCY. WILL HE SELL OFF THE AIRLINE PIECE BY PIECE OR WILL HE FOLLOW THROUGH ON HIS STATED INTENTION TO MAKE EASTERN PROFITABLE ON A SMALLER SCALE?

THE POSSIBILITY EXISTS THAT HIS TRUE INTENTION IS NOT TO OPERATE A DOWNSIZED EASTERN AIR LINES AT ALL, BUT TO, IN FACT, LIQUIDATE EASTERN, AND, THEREBY, ELIMINATE A COMPETITOR OF CONTINENTAL AIRLINES. ASIDE FROM THE OBVIOUS IMPACT ON EASTERN EMPLOYEES, LIQUIDATION WOULD FURTHER INCREASE CONCENTRATION IN THE INDUSTRY AND CREATE AN EVEN LARGER AIRLINE OLIGOPOLY THAN ALREADY EXISTS. THIS POTENTIAL LIQUIDATION DOES NOT BODE WELL FOR THE DEREGULATED MARKETPLACE.

WHAT WE DO KNOW IS THAT FRANK LORENZO HAS ANNOUNCED HIS INTENTIONS TO SELL OFF AT LEAST $1.8 BILLION OF EASTERN'S ASSETS. WHETHER HE WILL SELL MORE IS UNCERTAIN AT THIS POINT. WE HAVE TO WONDER WHETHER AFTER THIS SELL-OFF OF ASSETS, EASTERN CAN OPERATE SUCCESSFULLY, OR WHETHER THIS ACTION SIGNALS THE START OF LIQUIDATION. SOME OF THESE ASSET SALES INVOLVE ROUTE RIGHTS WHICH EXIST BECAUSE THEY HAVE BEEN CONFERRED BY GOVERNMENTAL ACTION. DOES FRANK LORENZO HAVE THE RIGHT TO SELL THESE RIGHTS OR IS IT IN THE PUBLIC INTEREST THAT THE GOVERNMENT RECLAIM THEM?

WITH THESE CONCERNS IN MIND, THIS HEARING SHOULD FOCUS ON WHETHER THE DEPARTMENT OF TRANSPORTATION SHOULD INTERVENE AT THIS POINT AND CONTACT THE BANKRUPTCY COURT TO REQUEST A DELAY IN THE APPROVAL OF FURTHER SALES OF EASTERN ASSETS UNTIL IT HAS HAD AN OPPORTUNITY TO DETERMINE IF THE PUBLIC INTEREST IS SERVED BY A DOWN-SIZED OR NON-EXISTENT EASTERN AIR LINES.

SO FAR, THE BANKRUPTCY COURT IS PERMITTING FRANK LORENZO TO SELL OFF ASSETS AND IS NOT ENTERTAINING ANY NEW OFFERS FOR INVESTORS INTERESTED IN PURCHASING EASTERN.

HOWEVER, I THINK IT IS WORTH NOTING THAT AN OFFER MADE BY JOE RITCHIE, HEAD OF THE OPTIONS TRADING COMPANY, CHICAGO RESEARCH AND TRADING GROUP, MIGHT BE A VIABLE ALTERNATIVE TO WHAT FRANK LORENZO SAYS THAT HE WILL BE DOING. THE RITCHIE PROPOSAL, AS I UNDERSTAND IT, WOULD PROVIDE FOR EMPLOYEE OWNERSHIP OF PART OF THE AIRLINE. THAT CERTAINLY WOULD HAVE APPEAL FOR EASTERN'S EMPLOYEES, WHO, AFTER ALL, WANT TO SAVE THE AIRLINE, NOT KILL IT.

YET, AS IMPORTANT AS A HEALTHY AND COMPETITIVE EASTERN AIR LINES IS TO ITS EMPLOYEES, THIS NATION AND THE FLYING PUBLIC ALSO HAVE A MAJOR INTEREST IN THIS MATTER.

IT SERVES THE INTEREST OF NO ONE TO LOSE EASTERN'S COMPETITIVE AIR SERVICE AND TO DECREASE COMPETITION IN THE AIRLINE INDUSTRY. IN TODAY'S CONCENTRATED INDUSTRY ENVIRONMENT, EIGHT CARRIERS ACCOUNT FOR OVER 90% OF THE TRAFFIC. WE KNOW, AS WELL, THAT FARES AT HIGHLY CONCENTRATED AIRPORT HUBS ARE MUCH HIGHER THAN AT MORE COMPETITIVE HUBS. WERE EASTERN TO DROP COMPLETELY OUT OF THE PICTURE, THE SITUATION WOULD ONLY WORSEN.

CERTAINLY EASTERN'S COMPETITORS HAVE NOT BEEN IDLE DURING ALL OF THIS. INDICATIONS ARE THAT THEY HAVE BEEN ABLE TO ACCOMMODATE EASTERN'S PASSENGERS WITH MODERATE INCREASES IN NONSTOP AND ONE-STOP FLIGHTS AND POSSIBLY SOME INCREASE IN LOAD FACTOR ON EXISTING FLIGHTS.

TRANSPORTATION SECRETARY SAMUEL SKINNER HAS EXPRESSED GREAT CONCERN OVER MAINTAINING COMPETITION WITHIN THE U.S. AIRLINE INDUSTRY. SO, IT IS APPROPRIATE THAT DURING THIS HEARING, WE CONSIDER WHETHER THE DEPARTMENT OF TRANSPORTATION AND THE DEPARTMENT OF JUSTICE SHOULD INTERVENE IN THIS MATTER TO MAKE CERTAIN THAT THE PUBLIC INTEREST IS PROTECTED. THESE AGENCIES, AS WELL AS THE CONGRESS, NEED TIME TO CONSIDER THE GRAVE PUBLIC CONCERNS RAISED BY EASTERN'S BANKRUPTCY. WE SHOULD CONSIDER TODAY'S HEARING THE FIRST, NOT THE LAST STEP, IN OUR DELIBERATIONS ON THIS MATTER.

I THINK THAT ALL OF US WOULD AGREE THAT THE PUBLIC INTEREST WOULD BEST BE SERVED BY THE OPERATION OF EASTERN AIR LINES AT FULL CAPACITY AND FULLY COMPETITIVE IN TODAY'S DEREGULATED ENVIRONMENT. THAT CERTAINLY SHOULD BE OUR GOAL.

THANK YOU AGAIN, MR. CHAIRMAN.

Mr. **Oberstar**. I thank the gentleman for his statement, and very succinct summary of the issues at hand.

The Chair now recognizes the gentleman from Georgia. Mr. Lewis.

TESTIMONY OF HON. JOHN LEWIS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF GEORGIA

Mr. **Lewis**. Thank you very much, Mr. Chairman. Mr. Chairman, and my colleagues of the subcommittee, I commend you for holding this hearing to examine the issues involved in the Eastern Air Line's reorganization under Chapter 11 of the bankruptcy code.

This is a matter of great concern to the good people of my congressional district. As you know, my district includes Atlanta and many of its suburbs. Thousands of Eastern workers, as well as shippers, suppliers, vendors, and other satellite industries, that depend on the commercial activities generated by Hartsfield International Airport and Eastern Air Lines, are depending on the Bankruptcy Court actions.

It was early March, just prior to the machinists strike, and Eastern filing for bankruptcy under Chapter 11, when you, Mr. Chairman, initiated a letter which was signed by more than 200 of our colleagues, to urge President Bush to establish a presidential emergency board to investigate the dispute between Eastern and its machinists union, in an effort to avoid a strike.

When it became clear and open that the President was not going to appoint a presidential emergency board, you, again, took the lead. You took the initiative, with the Chairman of the full Committee on Public Works and Transportation, Mr. Anderson, and introduced H.R. 1231 to require the President to act.

I, along with a number of my colleagues on this subcommittee, was original co-sponsor of this legislation. The Aviation Subcommittee and the full committee moved with dispatch and reported this bill to the Floor.

The House leadership responded to the emergency situation and scheduled immediately the bill for Floor action. On March 15th, less than two weeks after the strike began, the bill passed the House, 262 to 167.

Unfortunately, the Administration strongly opposed this legislation and the Republican leadership in the Senate was successful in blocking the bill in that body.

The Administration argument against the presidential emergency board bill was that it would prolong the impasse between Eastern and the union. For as much as 26 days nothing would be done to settle or to end the strike.

Also the Administration argued that the parties should be free to work out this dispute without outside or governmental interference.

Well, Mr. Chairman, we all know that this strike has exceeded the 26 days. In fact it is now in its 118th day, and, to my knowledge, there is no settlement in sight. There is no light, no light, at the end of this dark tunnel.

The Eastern strike has put a double whammy on the Atlanta area economy. It has put thousands of our citizens out of jobs, and has stopped the influx of much-needed money.

Hartsfield International Airport was ranked number one in the country in terms of air traffic. Now, because of the Eastern strike, Hartsfield's ranking fell to number three.

When you talk about air traffic, you are really talking about the number of people who visit the area. You are talking about the amount of money that is pumped into the city's economy. You are talking about the second-most important industry in the metropolitan Atlanta area—the tourism industry.

You are really talking about the economic viability of a metropolitan area. The Eastern strike is hurting Atlanta's economy. Because of the Eastern strike, my city's economy is not as vital as it once was.

Eastern employees, people in my district, cannot pay their bills. They are losing their homes. They cannot afford day-care for their children. They cannot feed their children. They cannot afford to buy clothes. Their cars are being repossessed.

The pressure the strike is putting on families has been unbearable. Almost impossible in many cases. Families are falling apart. People are falling apart.

Mr. Chairman, I am sad to say that there was a suicide of a machinist in Atlanta, recently, who could not pay his bills.

One woman, an Eastern flight attendant, called my office to say, just a few days ago, that her husband had left her, that her son's performance in school has fallen drastically, and that she had been threatened with foreclosure.

She has nowhere else to turn but to us, to this Congress. We have got to do something to help these hard-working people. We have an obligation, a moral obligation to come to their rescue.

In the meantime, it appears that Eastern leadership has embarked on a course to sell Eastern assets under the guise of a reorganization plan to restore a scaled-down version of the airline.

I believe this plan is one that is designed to bring about the liquidation of Eastern. Mr. Chairman, I hope that our hearing today will give this committee and the Congress a full picture of what is happening to Eastern Air Lines and its 31,000 employees.

I believe that once the committee hears the testimony today, it will conclude that the process under way in the Bankruptcy Court is nothing more than a fire sale of a major airline.

It is a liquidation being disguised as a reorganization. I am hopeful that this hearing will prod the Congress to act to ensure the survival of Eastern Air Lines. I want Eastern to emerge as a whole, with all of its employees going back to work. I want them to go back to work in an environment that engenders dedication, pride, and hope for the future.

The Congress can make this possible. I want to thank you, Mr. Chairman, for being so patient with my testimony.

Mr. OBERSTAR. I thank the gentleman. You have painted, in vivid words, the painful human chapter of bankruptcy.

When LTC Steel went into bankruptcy, it affected Reserve Mining Company in my congressional district, in two remote communities on the edge of the wilderness near the Canadian border.

and the same human experience pattern was followed there, that you have described in the urbanized Atlanta area. That is the real tragedy.

The gentleman from Georgia. Mr. Jones.

TESTIMONY OF HON. BEN JONES, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF GEORGIA

Mr. JONES. Thank you, Mr. Chairman. Mr. Chairman, and my colleagues on the Aviation Subcommittee, I wish to thank you for holding these hearings on these crucial issues which exist Eastern Air Lines' Chapter 11 case, and I thank you very much for giving me the opportunity to testify.

The Fourth District of Georgia which I represent, which I have the privilege to represent, includes urban, suburban and rural areas east and northeast of Atlanta.

The Atlanta area is an ancient crossroads. The Chattahoochee River was the traditional border between the Creek and the Cherokee Nations. Over the centuries, the Native Americans made trails which followed natural paths of least resistance to trading spots along the river. The paths became the first roads used by white trappers, traders, and the early white settlers. As late as 1830, the area where metropolitan Atlanta now stands was Indian territory. Then came the railroads, and Atlanta's natural geographic location led to its becoming the major junction of the Southeast. Where young Cherokee braves once brought hides to trade for precious stones, railroads, interstate highways, and major airlines now intersect, creating a city that was first, a marketplace for Georgia, then the hub of the Southeast, and is now an international crossroads for transportation, communication and high technology.

Metropolitan Atlanta's economy is vital today because its transportation industry has been vital. In the Atlanta area, Eastern Air Lines has contributed to the employment of some 7,000 citizens. In my district, the 4th District of Georgia, almost 900 people, representing 900 families, are currently not working because of the situation at Eastern. The absence of Eastern from Atlanta's transportation industry will result in the loss of an estimated $600 million to our local economy this year.

This loss has prompted Atlanta's Mayor, Andrew Young, to write to Judge Lifland, urging the restoration of Eastern to full operations. It has prompted our Governor, Joe Frank Harris, to issue a proclamation calling upon the Bankruptcy Court and all concerned parties to restore Eastern to its full operations.

Here, in Congress, along with my Georgia colleagues John Lewis and Newt Gingrich, and many of you, I have co-sponsored House Resolution 162 calling for the restoration of Eastern to full operations, and H. Res. 141, urging the appointment of a trustee.

This committee has been tireless in its efforts to call attention to the situation at Eastern, beginning with the Chairman's letter to the President urging the appointment of a presidential emergency board, and the subsequent House passage of H.R. 1231, a route which I feel should have been taken.

We are here today, Mr. Chairman, because in spite of all of these efforts Eastern Air Lines is in the Bankruptcy Court where its

Chairman, Frank Lorenzo, is continuing his practice of dismantling this once profitable and much beloved airline.

Mr. Lorenzo is conducting his dismemberment of Eastern under the guise of Chapter 11 of the United States Bankruptcy Code, which allows a debtor, acting in good faith, to seek temporary respite from the demands of his creditors' claims while he reorganizes his business.

The debtor's good faith is an essential premise of the right to Chapter 11 protection, and, Mr. Chairman, that good faith has not been evidence in the conduct of Frank Lorenzo before or since he took Eastern Air Lines into bankruptcy.

Mr. Lorenzo's control of both Eastern Air Lines and Continental Airlines, through his control of Texas Airlines, has created problems that cannot be ignored. In the words of David Shapiro, the examiner appointed by Judge Lifland, "Texas Air's decision to operate Eastern and Continental as separate subsidiaries may be justifiable from a business standpoint, but it has given rise to a web of personal and financial interrelationships among the four corporations and their management that create substantial conflicts of interest in this case."

I appreciate Mr. Shapiro's presence at today's hearings and I hope he will shed further light on this very real and very serious conflict of interest.

Mr. Chairman, the bankruptcy court always has a duty to protect the debtor's estate for the benefit of creditors, employees, and shareholders. When a situation exists in which the practices of the debtor may result in the irrevocable loss of a major player in America's transportation industry, I believe the Bankruptcy Court has an obligation to consider, as well, the public interest in the continuation of competition in the industry.

And when 25,000 machinists, flight attendants, and pilots cannot, in good conscience, participate in flying airplanes as long as one particular man is calling the shots, but are willing, and indeed, eager, to make very significant concessions to a new owner in order to get their beloved airline back in the sky, I think the Bankruptcy Court has additional obligations as well.

The court then has the obligation to recognize that the remarkable good will that these employees have for their airline will translate, in very real terms, to the long-term benefit of Eastern and its creditors. It has the obligation to recognize that this good will is depleted each time Frank Lorenzo is permitted to sell valuable assets of Eastern. And that this good will is an asset, that is the essence of the "ongoing concern," value of the airline.

William F. Buckley wrote in a recent column that, quote:

> Leadership needs to be shown by the bankruptcy judge who is properly guided b the long-term prospects for creditors, which are improved by a renascent airlin rather than by the sale of its nuts and bolts.

I share that sentiment, and it is my sincere wish that this hearing will help direct the kind of attention to this painful situatio which will encourage the preservation of Eastern Air Lines for th benefit of all parties who have an interest in seeing it fly, and fo the benefit of the American public, which is correctly concerne with seeing American companies operating in a competitive env ronment, and in a productive partnership of management and labor.

So I commend the Chairman and the subcommittee for their efforts in accomplishing this goal and I thank you.

[Mr. Jones' prepared statement follows:]

June 29, 1989

Testimony of Ben Jones, Representative, 4th District of Georgia

Mr. Chairman and my colleagues on the Aviation Subcommittee, I wish to thank you for holding these hearings on the crucial issues which exist in Eastern Airlines' Chapter 11 case, and I thank you for giving me this opportunity to testify.

The district which I have the privilege to represent includes urban, suburban and rural areas east and northeast of Atlanta. The Atlanta area is an ancient crossroads. The Chattahoochee River was the traditional border between the Creek and the Cherokee Indian Nations. Over the centuries, the Native Americans made trails which followed natural paths of least resistance to trading spots along the River. The paths became the first roads used by white traders, trappers and the early white settlers. As late as 1830, the area where metropolitan Atlanta now stands was Indian territory. Then came the railroads, and Atlanta's natural geographic location led to its becoming the major junction of the Southeast. Where young Cherokee braves once brought hides to trade for precious stones, railroads, interstate highways and major airlines now intersect, creating a city that was first a marketplace for Georgia, then the hub of the Southeast, and is now an international crossroads for transportation, communications and high technology.

Metropolitan Atlanta's economy is vital today because its transportation industry has been vital. In the Atlanta area, Eastern Airlines has contributed to the employment of some 7,000 citizens. In my district, the 4th District of Georgia, almost 900 people are currently not working because of the situation at Eastern. The absence of Eastern from Atlanta's transportation industry will result in the loss of an estimated $600 million to our local economy this year. This loss has prompted Atlanta's Mayor, Andrew Young, to write to Judge Lifland urging the restoration of Eastern to full operations. It has prompted our Governor, Joe Frank Harris, to issue a proclamation calling upon the Bankruptcy Court and all concerned parties to restore Eastern to its full operations. Here in Congress, along with my Georgia Colleagues John Lewis and Newt Gingrich, I have co-sponsored H.Res. 162, calling for the restoration of Eastern to full operations, and H.Res. 141, urging the appointment of a trustee. This Committee has been tireless in its efforts to call attention to the situation at Eastern, beginning with the Chairman's letter to the President urging the appointment of a Presidential Emergency Board, and the subsequent House passage of H.R. 1231, a route which I feel should have been taken.

We are here today, Mr. Chairman, because in spite of all these efforts, Eastern Airlines is in the bankruptcy court, where its Chairman, Frank Lorenzo, is continuing his practice of dismantling this once-profitable and much beloved airline. Mr. Lorenzo is conducting his dismemberment of Eastern under the guise of Chapter 11 of the United States Bankruptcy Code, which allows a debtor acting in good faith to seek temporary respite from the demands of his creditors' claims while he reorganizes his business. The debtor's good faith is an essential premise of the right to Chapter 11 protection, and Mr. Chairman, that good faith has not been evident in the conduct of Frank Lorenzo before, or since, he took Eastern into bankruptcy.

Mr. Lorenzo's control of both Eastern Airlines and Continental Airlines, through his control of Texas Airlines, has created problems that cannot be ignored. In the words of David Shapiro, the examiner appointed by Judge Lifland, "Texas Air's decision to operate Eastern and Contenental as separate subsidiaries may be justifiable from a business standpoint, but it has given rise to a web of personal and financial interrelationships among the four corporations and their management that creates substantial conflicts of interest in this case." I appreciate Mr. Shapiro's presence at today's hearing, and I hope he will shed further light on this very real, and very serious, conflict of interest.

Mr. Chairman, the bankruptcy court always has a duty to protect the debtor's estate for the benefit of creditors, employees and shareholders. When a situation exists in which the practices of the debtor may result in the irrevocable loss of a major player in America's transportation industry, I believe the bankruptcy court has an obligation to consider as well the public interest in the continuation of competition in the industry. And when 25,000 machinists, flight attendants and pilots, cannot, in good conscience, participate in flying airplanes so long as one particular man is calling the shots, but are willing--and indeed eager--to make very significant concessions to a new owner in order to get their beloved airline back in the sky, I think the bankruptcy court has additonal obligations as well.

The court then has the obligation to recognize that the remarkable goodwill that these employees have for their airline will translate in very real terms to the long-term benefit of Eastern and its creditors. It has the obligation to recognize that this goodwill is depleted each time Frank Lorenzo is permitted to sell valuable assets of Eastern, and that this goodwill is an asset that is the essence of the "ongoing concern" value of the airline. William F. Buckley wrote in a recent column that "leadership needs to be shown by the bankruptcy judge, who is properly guided by the long-term prospects for creditors, which are improved by a renascent airline rather than by the sale of its nuts and bolts."

I share that sentiment, and it is my sincere wish that this hearing will help direct the kind of attention to this painful situation, which will encourage the preservation of Eastern Airlines for the benefit of all parties who have an interest in seeing it fly, and for the benefit of the American public, which is correctly concerned with seeing American companies operating in a competitive environment, and in a productive partnership of management and labor. I commend the Chairman and this Subcommittee for their efforts in accomplishing this goal.

Mr. **Oberstar**. At this point the Chair would ask unanimous consent to include in the record the statement by Harry Johnston, a member of Congress from the 14th District of Florida. Without objection, so ordered.

[Mr. Johnston's prepared statement follows:]

Written Testimony Submitted to the HOUSE OF REPRESENTATIVES

Committee on Public Works and Transportation

Subcommittee on Aviation

June 29, 1989

Harry Johnston, Member of Congress

14th District of Florida

29 June 1989

On April 26, Congressman Porter Goss and I introduced House Resolution 141, which reflects the feelings of the many Americans who have been both directly and indirectly affected by the dispute between Eastern Airlines and its unions. Our resolution expresses the sense of the House of Representatives, that the negotiations for the sale of the company should not be brought to the brink of completion, only to break down over the question of who will run Eastern in the meantime. The resolution encourages the Bankruptcy Court to appoint an independent Trustee to oversee operations until the transfer of control to the new owner is complete. To date, 48 of our colleagues have joined us in expressing this same feeling by their cosponsorship of House Resolution 141. Senator Bob Graham of Florida introduced similar legislation expressing the sense of the Senate, which passed in that body overwhelmingly.

As Bankruptcy Judge Burton Lifland himself said, "Eastern has remained too long in the emergency room and is hemorrhaging at the rate of more than one million dollars a day." I share these feelings of urgency and maintain that the healing process is long overdue.

The disappointment brought on by the last-minute failure of the Ueuberroth deal was especially biting, given the true spirit of compromise characterized by the agreements worked out between labor and management. It is this frustration that I share with the pilots and machinists who reside in my district, throughout the state of Florida, and throughout the country.

Therefore, in considering the effects that the bankruptcy court's actions will have on the public interest, I urge the Subcommittee to recognize that the following Members have joined me in expressing their belief that the restoration of Eastern Airlines to full operations would best serve the public interest. The full restoration would not only be in the best interest of the creditors, employees, and customers of Eastern Airlines, but in the best interest of the economies of the communities, states, and regions of the country that Eastern Airlines serves.

Goss, Bennett, Nelson (FL), Smith (FL), Pepper,
Shaw,
Fascell, Gingrich, Frank, Lewis (GA), Crockett,
Jones (GA), Berman, Hutto, Porter,
Mavroules, Grant, Darden, Morrison (CT), Donnelly,
Morella, Mrazek, Patterson, Kostmayer, Saxton,
James, Parker,
Atkins, Mineta, Cardin, Bentley, Gordon, Quillen,
Williams, Rowland (CT), Callahan, Walgren, Henry,
Browder, Bosco, Ackerman,
Wolf, Fauntroy, Thomas (GA), Markey, Buechner,
Price, McMillen, Goodling, Pallone

101st CONGRESS
1st Session

H. RES. 141

Relating to the restoration of Eastern Airlines

IN THE HOUSE OF REPRESENTATIVES

April 26, 1989

Mr. Johnston of Florida (for himself, Mr. Goss, Mr. Bennett, Mr. Nelson of Florida, Mr. Smith of Florida, Mr. Pepper, and Mr. Shaw) submitted the following resolution; which was referred to the Committee on the Judiciary

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RESOLUTION

Relating to the restoration of Eastern Airlines.

Whereas the operations of Eastern Airlines have been substantially shut down since March 4, 1989, by a strike by the International Association of Machinists with the support of pilots and flight attendant unions;

Whereas Eastern Airlines filed a petition under chapter 11 of the United States Bankruptcy Code on March 9, 1989;

Whereas Texas Air Corporation, which controls Eastern Airlines, had negotiated for the sale of Eastern Airlines;

Whereas the organized employees of Eastern Airlines had agreed to provide a potential new owner with wage and work rule concessions totaling more than $200,000,000 annually for 5 years in return for a 30 percent equity share in the new company;

Whereas the sale agreement has expired for failure of the parties to agree on the management of Eastern Airlines until a new owner could assume control;

Whereas the deregulation of the airline industry by Congress was predicated on the anticipated continued existence of strong, independent airlines, such as Eastern Airlines;

Whereas the United States Bankruptcy Court has the power to appoint an independent trustee to manage Eastern Airlines' return to operation during the interim period, leading up to the consummation of the sale agreement and transfer of control to a potential owner; and

Whereas the return of Eastern Airlines to full operation is in the public interest and in the best interest of the creditors, employees, and customers of Eastern Airlines as well as the economies of the communities, States, and regions of the country that Eastern Airlines serves: Now, therefore, be it

Resolved, That it is the sense of the House that the United States Bankruptcy Court and all involved parties should facilitate the prompt and safe restoration of Eastern Airlines to full operations through all appropriate action, which may include appointment of an independent trustee, pending sale of the company.

Mr. OBERSTAR. I thank the gentleman from Georgia, Mr. Jones, for his very thoughtful, very pointed testimony, and for that bit of history that I had not known earlier about the State. I have no questions and yield to the gentleman from Pennsylvania. Mr. Clinger.

Mr. CLINGER. I am just very pleased to join you in thanking our panel for their very personal and obviously heart-felt concerns about this issue, and we welcome your testimony and welcome your suggestions. Thank you.

Mr. OBERSTAR. Mr. Kolter.

[No response.]

Mr. OBERSTAR. The gentleman from the Virgin Islands.

Mr. DE LUGO. Well, thank you very much, Mr. Chairman. I want to commend all the witnesses for their statements today and I want to say that I associate myself with your statements and with your concern. This strike is also impacting my district. I have three major airlines that come into my district in the United States Virgin Islands. Eastern Air Lines was the largest of them all, in number of seats, prior to the strike, and as you know, my district is totally dependent on tourism.

Prior to the strike there were four flights a day into the Virgin Islands. There was a minimum capacity of 616 seats and a maximum capacity of 723 seats, and now, we are down to two flights a day when they fly, with a minimum capacity of 260 seats and a maximum capacity of 275 seats.

My constituents who have worked all of their adult lives for Eastern, and been devoted employees, have been laid off, exactly the description that you have given here to this committee.

The suffering in human terms I think is the worst part of this. I think the description, John, that you gave of the impact on families is one that we have got to respond to, and I also was impressed by your statement, Ben, when you pointed out that the devotion and the commitment of the employees of Eastern, that this is a real asset, and that the Bankruptcy Court has got to take this into consideration.

[Mr. de Lugo's prepared statement follows:]

JUNE 29,1989

CONGRESSMAN RON DE LUGO

STATEMENT ON EASTERN AIRLINES HEARING

AVIATION SUBCOMMITTEE

I COMMEND CHAIRMAN OBERSTAR FOR HOLDING THIS HEARING TODAY. SINCE THE SENATE HAS NOT YET ACTED ON THE IMPORTANT LEGISLATION ON THIS MATTER REPORTED BY THIS COMMITTEE AND WHICH PASSED THE HOUSE IN MARCH, IT IS IMPORTANT THAT WE TRY TO LEARN WHAT IS HAPPENING TO THIS AIRLINE, IT'S EMPLOYEES, AND THE CUSTOMERS AND COMMUNITIES SERVED BY EASTERN.

FURTHERMORE, EASTERN IS ONE OF THE 3 MAJOR LINES SERVING THE U.S. VIRGIN ISLANDS. IT CARRIES MORE PASSENGERS TO AND FROM THE ISLANDS THAN ANY OTHER AIRLINE. AS ALL OF YOU KNOW, TOURISM IS TH LIFE-BLOOD OF THE ISLANDS, SO THE RESOLUTION OF THIS STRIKE AND TH FUTURE OF EASTERN AIRLINES IS EXTREMELY IMPORTANT TO MY CONSTITUENTS IN THE VIRGIN ISLANDS.A YEAR AGO THIS MONTH THERE WE 4 FLIGHTS A DAY TO THE ISLANDS WITH A MINIMUM CAPACITY 616 SEATS AND A MAXIMUM CAPACITY OF 723 SEATS. THIS YEAR AFTER THE STRIKE THERE ARE 2 FLIGHTS A DAY WITH A MINIMUM CAPACITY OF 260 SEATS AN A MAXIMUM CAPACITY OF 275 SEATS.

I ALSO NOTE WITH GREAT INTEREST THAT EASTERN'S POTENTIAL PLAN BE OFFERED TO THE BANKRUPTCY COURT WOULD INVOLVE SELLING THE ROUT AND ASSETS USED TO SERVE SOUTH AMERICA, THE CARRIBEAN, AND CANADA.THIS WOULD CERTAINLY DASH ALL HOPES OF RESTORING THE LEVEL OF SERVICE WE NEED IN THE VIRGIN ISLANDS.

FINALLY, I NOTE WITH KEEN INTEREST THAT ONE POTENTIAL BUYER OF EASTERN WOULD RETAIN THE MIAMI HUB AND KEEP EASTERN'S SERVICE TO THE CARIBBEAN AND SOUTH AMERICA. IN THIS CONNECTION, LET ME JUS SAY THAT HOWEVER ALL OF THIS IS RESOLVED, IT IS VERY IMPORTANT T WE HAVE THE LEVELS OF SERVICE RESTORED WHICH WE ONCE ENJOYED IN VIRGIN ISLANDS.

AGAIN, MR. CHIARMAN, THANK YOU FOR HOLDING THIS HEARING. IT'S APPROPRIATE FOR THIS COMMITTEE TO FIND OUT THE STATUS OF EASTERN AIRLINES TODAY AND ITS FUTURE.

Mr. de Lugo. Now do I understand, Mr. Lewis, that you view the reorganization plan that has been put forward by Mr. Lorenzo as simply a plan to liquidate the airline?

Mr. Lewis. That is my view, Ron. You know, people may disagree with it, but that is my view, that is my perception, that it is only a disguised effort to get rid of the airline.

I think that this man has a history of doing these types of things, so it would not be unusual or out of the ordinary.

Mr. de Lugo. Well let me say, Mr. Chairman, for the record, that I note that in the plan that is put forward, that Lorenzo is telling the Bankruptcy Court that he would like to sell off routes and assets.

Some of the routes that he would sell off would be those to South America, the Caribbean and Canada. And I also note, with keen interest, that one potential buyer of Eastern would retain the Miami hub and would keep Eastern's service to the Caribbean and South America.

So I hope that this will be taken into consideration by the Bankruptcy Court.

Mr. Oberstar. The gentleman's time has expired. Mr. Shuster.

Mr. Shuster. Thank you, Mr. Chairman. I have just one question of Congressman Gingrich, and we certainly appreciate all of your testimony.

I understand, Newt, that you wrote to the Secretary of Transportation pointing out the impact on competition and asking for him to intercede in the bankruptcy proceedings.

I wondered if you had any response.

Mr. Gingrich. We have not yet, to the best of my knowledge, heard back from them. We feel, strongly, that the Department of Transportation has two zones of intercession.

One is the impact on competition, as you point out, and the second is the question, to what degree does Lorenzo have the right to be selling routes which were given to Eastern Air Lines, as though they are personal property?

And to what degree does the Government have an obligation to intervene and say, wait a second, this is a matter of American Government concern and American Government allocation, and you cannot just ignore all the other factors.

So as a non-lawyer, I have been assured by attorneys that there is more than ample grounds for Secretary Skinner to intercede in the court, and to make this case, and to simply ask that the bankruptcy judge add this to the other concerns that have to be taken in account in looking at who should run Eastern Air Lines.

Mr. Shuster. Thank you.

Mr. Oberstar. I thank the gentleman. Mr. DeFazio.

Mr. DeFazio. No questions.

Mr. Oberstar. Mr. Costello.

[No response.]

Mr. Oberstar. Mr. Laughlin.

[No response.]

Mr. Oberstar. Mr. Valentine.

[No response.]

Mr. Oberstar. Mr. Bosco.

Mr. Bosco. Thank you, Mr. Chairman. I had a question for Mr Gingrich, too, along the same lines as Mr. Shuster's, and I agre with you that the Administration, particularly the Departments o Transportation and Justice, should play a much greater role tha they have been willing to.

Have you had similar contacts with the Department of Justic and, if so, could you tell us what——

Mr. Gingrich. We have not yet heard back. We have asked bot Departments to intervene, and, frankly, we have also suggested t the White House that the situation is different than it was severa months ago, and they were very cautious.

But now you have clear evidence that Mr. Lorenzo's primar strategy is to engage in behavior which clearly reduces the size Eastern, even if you put it in the best light—makes Eastern a les competitive airline, and does so in part by gaining assets, by sellin off routes that were assigned to Eastern by the U.S. Governmen

So I think there is a much stronger case now for the Executi Branch to get involved, and we hope, frankly, that this hearing wi be one more step in convincing them to take an active role in th court case.

Mr. Bosco. Do you feel that the Administration has in any wa changed its view as to whether a presidential emergency boa should be commissioned?

Mr. Gingrich. No. I still think that the President is not co vinced that the presidential emergency board is the right way go, but I do think that there has been a great deal more alarm e pressed over the way in which the bankruptcy judge and the pro ess with Lorenzo is going. That the hope that somehow econom pressure would bring the parties back together clearly has faile and the question now I think is whether the bankruptcy jud looks at the opportunity to have somebody like a Mr. Ritchie w is willing to work with the employees save the airline, and ke those routes the Government has assigned Eastern, or whether go down a path in which Mr. Lorenzo would, at best, drastica shrink the airline, and at worst, frankly liquidate it, in a w which may be helpful to Continental, but that dramatically— Mr. Shuster points out—dramatically worsens the competitive regulated environment.

So I do think there is a lot more edginess, frankly, at the Depa ment of Transportation than there was a while back. Frankly, o of our problems is that the nominee to be in charge of the corr part of the Justice Department, that would be looking at this qu tion of competition, is currently still in the Senate and has been approved, and so there is slightly less leadership in that a than they ought to have.

Mr. Bosco. Thank you very much.

Mr. Oberstar. Mr. Molinari.

Mr. Molinari. I have but one question of the panel. Aside fr the question of the viability of the respective offers, one of the s ous questions that have been raised is the safety issue presented the hiring of pilots. Eastern claims to have hired 600 pilots, but hear that only about a 100, a 108 have been certified by FAA.

So there is a genuine concern out there as to whether the pi being hired by Lorenzo are in fact qualified.

Now since you gentlemen represent so many people who are pilots and living in your area, have you any feedback on that? Has any concern been expressed to you about the safety presented by the new hires?

Mr. **Gingrich**. Let me comment as I have had several town hall meetings in which the allegation has been and we forwarded it to the Federal Aviation Administration, that there is some potential of having, for example, 727s that have both pilot and co-pilot with very, very minimal times. So you have a very low level of experience, and we learned in the Continental crash in Denver, that there are real problems if you have both the pilot and the co-pilot with very limited jet flight experience.

So we are pushing the FAA pretty hard to look at that. As you know, on some other maintenance things, FAA has been very tough with Lorenzo in this interim process, and in my judgment, they should continue to be very aggressive in ensuring that the traveling public's safety is paramount in the steps being taken by Mr. Lorenzo.

Mr. **Molinari**. I have no further questions.

Mr. **Oberstar**. Thank you. Mr. Payne.

[No response.]

Mr. **Oberstar**. Mr. Mineta.

Mr. **Mineta**. Mr. Chairman, just very quickly. The former, I believe senior vice president of Texas Air, is now a special assistant to the President of the United States of America.

Do you know whether or not in fact he has recused himself in all of the proceedings involving this matter before the White House?

Mr. **Gingrich**. As you can imagine, Mr. Mineta, this is an issue that I raised at the very beginning of this because it is an obvious potential conflict of interest, and I was assured personally that he has recused himself, and that he is not involved in any decision involving Eastern Air Lines.

Mr. **Mineta**. Would you like to buy a bridge? I would like to thank the panel very, very much for their fine testimony, and I appreciate it very much, Mr. Chairman.

Mr. **Oberstar**. Thank you. Mr. Ballenger.

[No response.]

Mr. **Oberstar**. The gentleman from Missouri.

[No response.]

Mr. **Oberstar**. The gentleman from New York.

Mr. **Towns**. Thank you very much, Mr. Chairman. I have no questions, but I would just like to thank the members of the panel for their outstanding testimony, and I share your concerns and I think that the information that you shared with us, has answered any questions that we may have had in the beginning. Thank you very much.

Mr. **Oberstar**. One final question of Mr. Gingrich who has had long experience in aviation, both on the Investigation and Oversight Subcommittee and on the Aviation Subcommittee itself. The downsized Eastern will have some 88 daily flights to 27 communities, and upgrading that—in the testimony we will hear later—and maybe 157 aircraft.

Do you think that is a real competitive airline in today's environment?

Mr. GINGRICH. Well, let me say—and I cherish the years I served with you on Investigations and Oversight, and then with both you and Mr. Mineta on Aviation—as you know over the years of hearings that both those subcommittees have held involving how Mr. Lorenzo airlines, I think you have to presume he will do whatever narrowly in his best interest without any significant regard for anybody else.

And we have had those fairly blunt hearings that you have chaired, and that Mr. Mineta has chaired, talking about this problem.

I think that you cannot measure an airline by the number of aircraft. There are small commuter airlines that work, that work very, very well. Airlines can grow through a phase, as for example, Piedmont and USAir have, where they keep acquiring it. What worries me about Eastern, as it is currently going, is that Mr. Lorenzo's management style is so systematically destructive, and he has been so unable, even at Continental, to make a profit, that it is very hard for me to see how he can be taken seriously in offering to rebuild a downsized Eastern Air Lines.

I think it is far more likely that his management style guarantees that he ultimately destroys the airline and then takes the profits which have been hidden at Jet Capital and Texas Air and simply either leaves the business or tries to see if he can keep Continental by itself.

I am very, very skeptical that his operational plan has any hope of succeeding.

Mr. OBERSTAR. Downsizing may simply mean downgrading from the status of a major carrier to a relatively small or mid-size regional or commuter carrier, which is not going to be contributin in the national air transportation scheme.

Mr. GINGRICH. Well, you can imagine a strategy which, in orde for the airline to survive, it had to do that. What I guess I am di turbed by, and what I hope the Department of Transportatio would bring to the bankruptcy judge's attention, is that there ar interest of the employees, there are interest to the communities, a Mr. de Lugo said, that would not be served.

There are interests of the Nation in having a competitive airli system, and if all other things are in any way equal, it would see to me that the operational plan which gave us a larger and healt ier, and more competitive Eastern, is the one the bankruptcy jud ought to favor.

That ought to be a factor in his consideration. That is clearly n the Lorenzo plan.

Mr. OBERSTAR. I thank the gentleman for those responses, and thank all three members of the panel for your contributions. Th have been very, very helpful.

We will proceed with our next panel consisting of Frank C. C lucci and Mr. Joseph Ritchie. Mr. Carlucci, Mr. Secretary, yo fame and previous service precede you. We welcome you to t committee. The subcommittee is not ordinarily in the business hearing testimony from Secretaries of Defense, even though it i former title you held, it is a pleasure and a privilege to have y here with us. You have won great respect from members of b sides of the aisle of your professional management of that great in budget size, of all Federal agencies, and we welcome your presentation today.

TESTIMONY OF A PANEL, CONSISTING OF FRANK C. CARLUCCI, JOSEPH RITCHIE, ACCOMPANIED BY RUSSELL THAYER, SENIOR VICE PRESIDENT, AIRLINE ECONOMICS INC., JAMES HARRIS, SHEARSON, LEHMAN, HUTTON, AND PAUL HOLT, CAMBRIDGE INTERNATIONAL PARTNERS

Mr. **Carlucci.** Thank you, Mr. Chairman, members of the subcommittee. It is indeed a pleasure for me to appear before you today on this subject of importance public interest.

My role in this undertaking would be limited to a temporary period as CEO, should the Ritchie proposal be successful, so I will perforce be brief with my testimony.

Shortly after Eastern filed under Chapter 11, I was interviewed as a potential examiner. The U.S. Trustee selected David Shapiro, a fine choice.

During the period when the Ueberroth proposal was under active consideration, Mr. Shapiro asked me if I would be willing to serve as trustee during the due-diligence period.

Viewing this as a public service, I agreed. As the committee is aware, the Ueberroth proposal aborted and consequently a trustee was not named.

Several weeks later, Joe Ritchie asked me if I would be willing to be interim CEO of Eastern should his bid succeed. Mr. Ritchie believed that my past experience as Secretary of Defense, managing an operation the size of the Pentagon, and the fact that I was acceptable to the unions, would help him put together a new management team.

We expect to hire the very best, experienced airline executives, and we believe that we will be able to attract the highest-quality management personnel.

This approach seemed to be acceptable to the creditors committee. In today's business climate, it is tempting to characterize the struggle over Eastern as a typical takeover fight. But that would be to misjudge the character and the intent of the Ritchie proposal.

As I have worked with him, I have come to recognize the depth of Joe Ritchie's social commitment. His concern is first for the workers and the public, with financial returns a secondary issue.

He has formed an alliance with the workers that is truly unique in its mutual understanding and dedication to common goals. While I do not underestimate the enormous management challenge restarting Eastern represents, the worker-management partnership Joe Ritchie has formed will certainly make this task easier.

The workers have shown extraordinary willingness to make financial sacrifices and the unions have stepped forward with unprecedented financial contributions.

I know of no business situations where the workers will have such a vested interest in making a success of the operation.

Joe Ritchie is a firm believer in employee participation, and he has demonstrated it in his own company, CRT. Ultimately, of course, employee enthusiasm translates into enhanced shareholder value. In my judgment, this approach is the only one that has a chance of restoring Eastern to its once-proud status, and of meeting the legitimate requirements of the traveling public.

I am very comfortable with this style of management. Indeed, I have tried to emphasize participatory management in my previous positions and I believe I can set clear goals for the airline, and work with Joe and the unions to get Eastern flying again, and to put together a permanent management team.

I would consider it a privilege to work with the Ritchie team and the union leaders and workers, many of whom I have come to know during this interim period.

Mr. Chairman, in my judgment time is short. If the situation is allowed to drift much longer, Eastern will almost certainly disappear as an airline. The Ritchie proposal is a viable alternative to slow liquidation and it certainly meets the public interest concerns of this subcommittee.

I commend you and the members of the subcommittee on your willingness to examine this issue in an impartial manner, and I thank you for allowing me to appear before you.

One final comment, Mr. Chairman, and members of the committee. As I got off the airplane yesterday at National Airport and walked past the picket line, a number of the pilots recognized me, and one of them shouted out, "Don't forget us."

And I reflected a bit on that and it seemed to me that the pilots out on that picket line, as well as the other people in the picket line were very similar in many respects to the people that I was in charge of in the Pentagon. Dedicated, committed people, many of whom come from military backgrounds.

As your colleagues pointed out earlier, these are people who have family problems but who are dedicated to their professional task, to a goal of making a productive contribution to society, and I would simply suggest to this committee that, indeed, we should not forget them.

I will be happy to answer questions, Mr. Chairman, but before doing so, I would like to turn the podium over to my friend, Joe Ritchie.

Mr. OBERSTAR. Thank you very much, Mr. Carlucci, and I appreciate your personal touch. I think as our colleague, Mr. Lewis, and other colleagues from Georgia did in their testimony, you have touched on an element that we all too often forget in discussions of broad public-policy issues, and that is people, the consequences for the daily lives of people whose work, livelihoods, and meaning in life is summed up in what they contribute to society through their work.

Mr. CARLUCCI. Thank you, Mr. Chairman.

Mr. OBERSTAR. Mr. Ritchie.

Mr. RITCHIE. Thank you, Mr. Chairman, members of the committee. I appreciate the invitation to address you.

Mr. OBERSTAR. Please pull the microphone closer.

Mr. RITCHIE. I would like to answer for you the most commonly asked question, which is why do I want to buy this airline. I am not an airline expert, I never have been, but I am a people expert.

My business, Chicago Research and Trading, has done very well by simply treating human beings the way I would like to be treated, and the putting one foot in front of the other, and with that philosophy we have started with a couple 100,000 in capital, and gone up to a couple 100 million. We have not had any losing years.

We have had a lot of fun doing it, and we have related to each other like family, which is the part in which I take a lot more pride than the financial success.

So when I looked at the Eastern situation, I looked at it like a people problem, fundamentally. Of course it is also a business problem, and we have experts here from Shearson, from Airline Economics, and we have retained another expert firm as well to answer those questions.

But fundamentally, it is a people problem. So I looked first at the people involved. There is a strike going on here. Why?

And as I looked, I could not believe what I saw. When you listen to people tell why they are striking, you can take everything they say with a grain of salt, if you assume that they are striking for more money.

But this equation is a little different than what we are used to. The pilots, against everybody's calculation, went out on strike without their contract in dispute, with nothing but financial risk, and no potential reward.

Pilots at the top end of the scale were making in the vicinity of $100,000 per year, and if they lose this gamble, they can go back into an industry where they can start at 20,000, maybe less, if they can start at all. The more senior ones may not be hireable at all.

At the lower end of the scale, new pilots, by crossing the picket line, can go from second officer to captain. Second officer is not the co-pilot; it is the guy that sits behind the two and wishes he could fly.

A process that normally would take 20 years of seniority, and they could have moved up by simply crossing the picket lines. The captains, by the way, would go back to work as second officers. And in the face of those odds, 95 percent of the pilots went out on strike and supported the machinists, the first time I know of where white collar has gone out and supported blue collar.

Also the first time I know of where they went out to save the company rather than to simply get more wages. If they were going out for money you could take what they say with a grain of salt, but they are not, and so I want to just read a couple things that have come in letters from them.

I have got a stack here of letters that I have received from these people. I have brought them all for your perusal. I have not culled any.

The tone of all of them is the same. In all these letters I have not seen the desire for higher wages mentioned once. There are recurring themes that come through repeatedly, that have to do with human dignity, with being treated with respect, and with saving the airline.

Here's a couple that just came in yesterday. Captain Richard Rogers from Arlington, Virginia.

> It is not a strike for more pay or better working conditions. It's a strike of righteous indignation. It's a strike against certain business practices. It's a strike to have

> a management with integrity. It's a strike to have the employees treated as assets rather than liabilities. It's a strike to have the employees be shown the respect of a fellow human being. Above all, it's a strike for employees to be treated with basic human dignity.

Here's another one, too, that just came in yesterday. Captain Shepherd from Georgia.

> For the first time in many years I am standing proud beside my fellow pilots in a cause that is right. Even if we lose Eastern and our jobs and careers, we are right and we're winners, for we're courageous enough to take a stand.

And this is a battle which—face it—they are underdogs. Their wives write letters, respecting their husbands for doing what they think is the right thing, and wives have a stake in this. They are not disinterested parties, when the income is going to go from 100,000 to 20,000.

One more letter that just came yesterday.

> My entire family, six of us, were employees of Eastern Airlines. We were all happy to be there and although we knew we would never be rich, we were comfortable and we did our work with pride. My family was in the airline industry long before Mr. Lorenzo was, and I've spent many bad-weather nights at the Atlanta airport consoling passengers to the wee hours of the morning when my shift was long over.
>
> What I did for Eastern I did because I loved my job and took special pride in being very good. I made many, many friends of the traveling public for Eastern. The employees of Eastern are probably some of the best in the industry because they always had to give out more than any major airline in order to keep the airline running.
>
> My family and I have a total of 165 years' seniority. We gave them the best of ou lives. I could cry about it, but in reality I feel a lot of pride for my fellow worker who are doing what should have been done a long time ago. We love Eastern an will make it great, but we want no part in tearing it down.

Again, sample these for yourselves. These themes run throug these letters, repeatedly. Now you may be asking, what does a this emotion have to do with the survivability of Eastern? It has lot to do with it, because the problem at Eastern has not bee originally, lack of capital or lack of airplanes. It has been lack the kind of relationship between management and labor th makes labor work.

And there are lots of ways to look at a business and what mak it survive, but I believe the main assets of any business are people. Our business is not one that uses a lot of equipment, or high investment. It is one that uses people, people, people, and you get that right you win and if you do not you will lose.

And the notion that by controlling them, squashing them, wri ing every last drop out of them, to have the lowest pay scale, is notion that a lot of American businesses have used, but it has worked well. It is not the one we have used, and I think it is w has killed Eastern.

I want to read one more quote. This is from a non-contract e ployee. It is from a woman who has been with Eastern 21 yea and it is not written to me. It is written to Mr. Frank Loren Texas Air Corporation.

There is no bitterness in this letter. There is no hatred. There no self-pity. There is anguish. There may even be anger. But right, pure human emotions—these letters in general have not generated into the hatred and self-pity kind of emotions that we look down on.

She says that her father, who passed away 2 years ago, came to this country when he was 17 years of age, was processed on Ellis Island, the Statue of Liberty was his beacon of hope and promise in the land of opportunity and freedom to exercise his God-given rights.

> He always taught me the value of the free enterprise system. You take care of your job and it will take care of you. My dad believed in the golden rule—do unto others as you would have them do unto you. There was reverence and dignity for the human person.
>
> My appeal to you, Mr. Lorenzo, is based on that culture, Spanish culture, incidentally, which reflects what your own father must have revered. You see, my father was born in Lacaruna, Spain, province of Galicia, the same province from which your father migrated to the United States.
>
> And just as I settled into thinking that we must appeal to each other with dignity, a large sign blazoned across the beautiful Manhattan sky—most nonstop flights to Florida. Continental. I became angry. This is Eastern's market. Eastern Airlines is headquartered in Miami. Eastern is 62 years of age.

And she goes on to talk, not about how she has been wronged, but about the pride in Eastern, again, which, is shot through these letters.

She had good reason to feel she was wronged. She worked as a volunteer after the strike to try to keep the airline in the air, and after doing 12-hour days as a volunteer worker on a 9-hour bus trip back home, found out of her "no-work" status when stopping to call in during one of the stops, arrived at Tampa, was given a check which bounced.

But as she goes on, she continues to focus on the things that made her proud of Eastern.

"Mr. Lorenzo, would you want to be treated this way? Regarding treatment, what about our valuable customers?" And she asks why customers who have bad tickets are told they are no good when the public, for a 5-minute delay, can get a free ticket now.

Twenty-one years. She was there through the long period when the employees had give-back programs so they could own part of the company. The period when productivity went through the roof for a while; when they felt like they participated.

She says,

> Through all our give-back programs we became the company, not owned, became. We are Eastern. We are a family. We have dignity. My personal belief is that our spirituality is grounded in our work. Solidarity of the human spirit in the workplace, asserting our dignity and yours.
>
> That message is ringing loud and clear to all working people in our country because it hits the cord of their own being. The Nation is caught up in it. Sending a message to corporate America that people are the most vital of all assets. Management has the responsibility and the power to enhance this dignity, not the power to diminish it. Please help us to save our airline for all 32,000 of us.

Like I say, the purpose of reading this is not to make this issue emotional. It is a business issue. I am a conservative, Midwestern businessman, but even some businessmen believe that if you want to run a business you have got to treat people right.

And I believe that is all these people want. They are striking, if you think about it, for lower pay, for harder work, for less work rules, for more risk taken by themselves. All the things that us conservatives have always told labor they should think about, and here they are doing it all at one time. That is why not only have left-wing liberals and Democrats supported this, but people as far to the right as Bill Buckley.

And that is why I am interested in it. Now, there are a lot of hard, cold, business questions about our business plan compared to the other, and so on, and I do not have time to get into all this. I think the tough questions have good answers and my concern is that you will not ask—that you will ask us tough questions. It is that you will not ask us the tough questions. Because my time does not permit me to go into it in my opening statement.

So if you can address questions about why we think our business plan is the right one, why we think the other one, or a plan like the other one would not fly, even with our fresh capital, we will be happy to answer those.

Mr. OBERSTAR. Thank you, Mr. Ritchie. Do any of your associates have comments, other than Mr. Carlucci?

Mr. RITCHIE. No, Mr. Chairman.

Mr. OBERSTAR. All right. We appreciate also your focus on the human element. That does touch a very responsive cord among all of us who are concerned, as we must be, about people issues.

In the context of the bankruptcy laws, let us suppose that the examiner agreed with you, and that yours, indeed, is the best proposal for ensuring the survival of Eastern.

How does the bankruptcy judge, and how does the examiner go about encouraging an unwilling debtor-in-possession, Mr. Lorenzo, to accept that proposal?

How important is it to have the creditors committee on your side, and are they on your side?

Mr. RITCHIE. Well, you are asking partly a legal question and partly a question about the creditors committee.

Mr. OBERSTAR. Please come up closer to the microphone. It is important that we hear you.

Mr. RITCHIE. The creditors committee has taken the position that the difficulty is not with the viability of the plan. The difficulty is with the legal problem, that no matter how viable it is, they do not have the power to force Mr. Lorenzo to sell the airline.

So it is not a plan issue. In fact to simplify this, with the creditors committee, what we have done is we have said, look, here are two ways of running this airline. We believe one works better, but to enable you to compare an apple with an apple, that is, our plan with Mr. Lorenzo's, we will allow you to force us to sell off the South American routes, and so on, if the facts, if the experience of actually running the airline—as opposed to the theoretical projections—do not verify what we are saying.

In the meantime we will infuse enough extra capital concessions, and so on, to cover your risk. So this has gotten missed in the whole comparison of these plans, but we have allowed this comparison to be made on an apple to apple basis, and we have asked if there is a single thing, comparing the plans in that way, in which ours is not superior, and we have not yet heard an answer to that.

There are a number of ways in which it is decidedly superior. There is fresh capital. There are wage concessions. There are work rules being given up.

There is a motivated work force, and there is a work force. And that allows a ramp-up that is much faster and broader. So we do not think there is really any comparison, and we would invite this committee to investigation, independently, the plans, or have the Department of Transportation check them out.

It is a hard issue to answer when no one will come forward and explain where our plans are inferior.

Mr. **Oberstar**. What is the creditors committee saying about your plan, and what influence does that have within the bankruptcy process?

Mr. **Ritchie**. Well, they have said that they find it interesting and constructive, but they feel that they cannot do anything at this point because they do not have the legal right to make things move in that direction.

Mr. **Oberstar**. Can they vote against Mr. Lorenzo's plan?

Mr. **Ritchie**. Legal questions. Frank, you would know more than I. Can they vote against the plan? The answer is yes, they can.

Mr. **Oberstar**. Have they been given an opportunity to do so?

Mr. **Seidel**. Not yet, Mr. Chairman. The way the process works, a debtor-in-possession such as Eastern Air Lines——

Mr. **Oberstar**. Please get to a microphone and identify yourself.

Mr. **Seidel**. Mr. Chairman, my name is Barry Seidel. I am with the firm of Levin, Weintraub and Krames, bankruptcy counsel for Mr. Ritchie.

Mr. **Oberstar**. Thank you.

Mr. **Seidel**. The way the process works, a debtor-in-possession is given 120 days to file its plan of reorganization.

During that period of time, the debtor-in-possession is the only party which can file that plan. Eastern Air Lines' exclusivity period, as we call it, would expire on July 7, I believe is the date. Eastern Air Lines has yet to file that plan.

I believe parties in the case believe that that plan will be filed by July 7th. If the plan is filed by July 7, the bankruptcy code says that the debtor-in-possession is given an additional 60 days to see if it can get acceptances to that plan.

That is what I believe you were referring to. The plan has to be filed. The creditors, then, stockholders as well, will be given an opportunity to vote on that plan. As the plan has not yet been filed, that process has not begun.

Mr. **Oberstar**. Have the creditors given any public indication of what their preference is? They play a very important role in this matter and we have heard very little from them. Any indication on their part might be decisive, one way or another, or at least influential.

Mr. **Seidel**. You are quite right. Unfortunately, the deliberations of a creditors committee are not oftentimes made public, and we have heard back-room discussions about what their positions are.

I do not know if they are present here today. Maybe that question should be addresed to them, but I cannot answer that.

Mr. **Oberstar**. Thank you.

Mr. **Seidel**. Thank you.

Mr. **Oberstar**. Mr. Ritchie, as I understand your proposal, it differs from Eastern's plan, in that Eastern would concentrate on Atlanta as a hub while you propose to retain Miami as a hub and retain the Latin America service.

Your view obviously is that Miami and Latin America are service points that can be profit centers for Eastern.

How do you reach that conclusion, and do you have plans for improving Eastern's service and financial routes in those markets?

Mr. RITCHIE. Well, let me give you my businessman "horse sense" answer for starters, and then experts can answer them with more particularity.

Mr. OBERSTAR. Be brief and to the point.

Mr. RITCHIE. Okay. We have hired not one expert, but Shearson, Cambridge Partners International, and Airline Economics, all three, to look at this very question.

We have no reason to be biased, one way rather than the other. I am putting my money on the line here, and obviously I want to go with the plan that has the best chance of not losing my money.

So that is the perspective I am coming from. As they look at the plans, you see something very clear, that really, fundamental economics would have told you you would see.

You have this thing called "critical mass," an industry that has large, fixed expenses, variable revenues, and as you bring down the number of airplanes you see the revenues coming down, and pretty soon they cross this line where you go into the red.

So they tell me, if you are going to buy this airline, you need a minimum amount of critical mass, and when you go much below 200 planes you are in big trouble fast. That is the simply "horse sense" look at it.

We have no reason not to run this as a trimmed-down airline, and we would be happy to if we thought it could survive. We think it cannot, even with fresh capital being infused.

Now some more technical. Russ Thayer.

Mr. THAYER. Let me give a more defined description of "critical mass." Since deregulation, the successful airlines have built hubs, and hubs are built on gathering your own traffic that used to come to you by interline traffic from other persons' systems.

It is now very necessary to have a certain level of critical mass. The difference in our plan includes the Miami gateway, Latin America, the Eastern Caribbean, Central America. All of this traffic flow comes from all over the Eastern system, about 10 percent. If you sell off those assets, that flow goes away and gets fractionalized over the other majors.

Every major is growing rapidly to improve its critical mass. Our basic concern as a consultant on this project is if Eastern sells any more assets, they will drop below that critical mass, and although the new Eastern will survive for a time, it will ultimately go out of business or be swallowed up.

Mr. OBERSTAR. The examiner has, though, indicated—and I will prolong just a moment—that he could not approve a scaled-down Eastern because the unions would not agree to it.

Mr. THAYER. We have not based our analysis on the number of people employed, or the number of airplanes operational, or the unions' opinions. What we have based our analysis on is airline economics in today's deregulated market, that has a very necessary factor of critical mass. I can site 100 examples if the time was here.

Mr. RITCHIE. Mr. Chairman.

Mr. OBERSTAR. Yes.

Mr. **Ritchie**. There is a further answer to that. The unions, because they want the airline to survive, do not want a trimmed-down airline either, simply because they think it will not survive. Well, there are other reasons as well, of course.

But they are willing to take that chance and put their money and their jobs where their mouth is on this point, by saying, let us try to run the airline the way we and our professionals tell us it should be run, and if it does not work the way we are projecting then we will trim it down.

In effect we will self-cannibalize ourselves to satisfy the creditors, not that we want to do it, not that we think it makes business sense, but it is one of those things you finally throw in as a desperation solution to an objection that you think makes no sense but you have no other way to answer, and that is the answer.

So the unions, while they think it is dumb from a business standpoint and from a job standpoint, are willing to do it simply to get over this hurdle.

Mr. **Oberstar**. Well, there really is not much difference, then, between 197 aircraft and 157 aircraft in your proposal, and Mr. Lorenzo's. What makes yours viable, then?

Mr. **Thayer**. I think there is quite a bit of difference, Mr. Chairman, the difference being that we include long, extensive routes that are not in their proposal. It keeps a very dynamic Miami gateway, and I stress the word "gateway".

This is important to this critical mass, the traffic flows on its system, and that is where we are coming from. All of that is necessary to survive in today's hubbing industry, with critical mass operators.

Mr. **Oberstar**. Mr. Thayer, for the record, I think it should be mentioned you have had previous experience in the airline industry, and I would like you to describe that.

Mr. **Thayer**. About 40 years; yes, sir.

Mr. **Oberstar**. In what capacity active?

Mr. **Thayer**. As president of Braniff in the older days, and as senior vice president, Operations, in Pan American World Airways.

Mr. **Oberstar**. Again, are these Latin America routes profitable, or potentially profitable routes, that make this proposal different from and more attractive than the plan of Mr. Lorenzo?

Mr. **Thayer**. They are very profitable routes. They are now, and that is why they are salable. They also are only operating about half of the authority in Latin America.

The reason they are profitable routes—there are really no highways and railways between the countries down there because of the Andean Range, and all the traffic on the west coast operation, which is the Eastern routes, is business travel. You say it when the Chilean grapes got contaminated.

It is a business market, very good yield, long haul, where airplanes make money.

Mr. **Oberstar**. Thank you. My time has expired. Mr. Clinger.

Mr. **Clinger**. Thank you, Mr. Chairman. Thank you, Mr. Ritchie, Mr. Carlucci, and gentlemen, for being here today to explain your plan and how it would work, and how it would enable Eastern to survive.

There is, however, a discrepancy, I think, or at least a disagreement on what constitutes a "critical mass" in terms of Eastern, and I wondered if you could explain that discrepancy.

As I understand it, the bankruptcy examiner has indicated that if there are no asset sales then he would anticipate that it would require an infusion of at least $300 million in new capital, and that he really was not terribly interested in looking at your plan unless there was at least $200 million on the table, and at the moment, as I understand it, we are talking in terms of about $100 million of new capital.

That is a pretty big difference between what he views as necessary, in terms of $200 million to $300 million, and $100 million. Are you suggesting that that differential can be overcome solely by virtue of the fact that you would have a motivated work force to accomplish this ramp-up?

Or are there other bases on which you feel that you do not need that much capital infusion?

Mr. RITCHIE. Yes. There is a lot more than $100 million. Actually, Jim Harris of Shearson should speak to that issue.

Mr. HARRIS. Congressman, my name is James Harris. I am a managing director with Shearson, Lehman, Hutton in New York and I am the financial advisor to Mr. Ritchie and the Ritchie Group.

I am not familiar with the examiner's statements as to the $300 million, but we have proposed in our plan to provide in excess o $100 million of new capital going in, a 100 of it on a very high-risk basis which has never been done before, to my knowledge, in bankruptcy, to restart the airline in effect, to get it flying, an then to raise new capital to bring Eastern out of bankruptcy at th end of the bankruptcy process.

The total needs that we estimate would be somewhere in th area of $300 million of financing, either debt or equity, to complet the reorganization process once the airline has been ramped up.

So there is $100 million of new financing going in, day one, start the airline, which would be high-risk capital. This would co vert into equity upon a successful reorganization.

Mr. CLINGER. So you anticipate that in the long run, howeve you would have an infusion of $300 million in capital?

Mr. HARRIS. Between $300 million and $400 million.

Mr. CLINGER. Okay. What about the question of the viability the Lorenzo plan? As I understand it, you and others will testi that this is merely a subterfuge for liquidation.

It is our understanding that in fact Eastern has employed pilo is engaged in a fairly ambitious training program for the pil that they have hired, investing a substantial amount of money training these pilots to assume positions in their organization.

Is that really consistent with the thought that they are planni to liquidate the airline? Would they really be investing these kin of resources if it was all a sham?

Mr. THAYER. I think to come around the other side of that qu tion a little, in order to keep the asset values up, I do not think y can announce a liquidation in its state right now. The asset valu as you know, as they are being sold, are going for higher than th asset value is being appraised.

As long as you keep it in a bidders market, it is high up. For example. Let me give you the example of a new 757 fresh off the Boeing line and costs in the neighborhood of $41 million.

They were able to sell a few of them the other day for $37 million, that are about 6-year-old airplanes. That is a fantastic maintenance of the price of the airplane because of its asset value in a bidding process.

So I think the effort to raise a small Eastern, in Lorenzo's plan, is an effort to keep up these values, so that they can move the assets at a high value.

Mr. CLINGER. So you are saying that it would be consistent, then, that they would be investing in pilot training and certification?

Mr. THAYER. Yes. Yes.

Mr. CLINGER. I see my red light has gone on. Just one question. Mr. Carlucci, it was indicated that you would become the interim CEO of this airline in the event that Mr. Ritchie's bid is successful. How long is "interim"? How long would you anticipate that you would be in the saddle, or in the cockpit?

Mr. CARLUCCI. Mr. Clinger, that would really depend on how long it would take us to put together a first-rate management team. My anticipation would be that that would probably be five to six months. We would work at it as assiduously as possible.

In fact we have already started to identify people. So my principal effort would be in getting it going and identifying that——

Mr. CLINGER. So your primary responsibility, then, will be to recruit and put in place an experienced team, professional team of airline experts?

Mr. CARLUCCI. I would see that as a principal responsibility, although obviously, you have to set the goals for the airline in the interim period and get the ramp-up going, and I think we have identified the technical expertise to do that.

Mr. CLINGER. Gentlemen, I thank you all very much for your appearance and testimony.

Mr. OBERSTAR. Thank you, Mr. Clinger. The gentleman from Pennsylvania. Mr. Kolter.

Mr. KOLTER. Thank you, Mr. Chairman. I have but one question for this panel. Mr. Ritchie, as I recall the last time this subcommittee met with Eastern Air Lines, the officials of Eastern Air Lines indicated that they were not able to meet the wage demands, that in fact were talking about the various airlines using the same unions, the same pilot unions, the same mechanic unions, yet they were not able to meet the same wage demands for their employees.

In order for your company to be effective, how would you do this? How would you handle this major problem that created and preempted a strike?

Mr. RITCHIE. The problem of their wage demands?

Mr. KOLTER. Yes.

Mr. RITCHIE. A very good question. In my experience in business, there are two main ways to bargain with people. One is the sort of bargaining where we utilize every ounce of power or leverage at our command to squeeze as much a percentage of the pie as possible for ourselves, so that it is a pure tug of war between you and me, if you are my partner.

The alternative is if we would prefer to work together like good friends, then I wind up saying, well, Mr. Kolter, gosh, you are entitled to at least 60 percent of this pie—even if I really think it is 50—just because by taking that kind of position the whole pie is going to be so much bigger that I am going to come out ahead.

And then you turn around and say, no, Joe, you are probably entitled to two-thirds of it.

Negotiations, it seems to me, tend to fall into one of those two categories. Every partnership I have been in—and I have been in a lot—has fallen into the second category every time.

When you approach people that way, they take a whole different attitude. I have approached the unions that way, and, surprise—they have come back and said they will work for far less than what they were asking for in their negotiations with Texas Air. Or with Eastern.

And that is basically the answer to how you solve the problem. How would I squeeze them down? I do not have to squeeze them down. I simply say, truthfully, it is a partnership I want here. Now you tell me, what do you want to work for in order to get this thing financed, in order to get the creditors on our side, in order to get bankers willing to go along with us?

And they come back with numbers far below what I would have thought appropriate. The first time I asked Charlie Bryan that question, he put a pencil to it, came back with a number, and his advisor almost fell off his chair. He said, "Charlie, you can't do that." And Charlie said, "Yeah, I think I can do that. Don't you realize we're talking about being part of this thing. Man doesn't live by bread alone and that's all these guys are interested in is being part of it, and when they're part of it they'll make concessions beyond what anybody believed possible."

And the reason is, they do not see them as concessions at all, because they are not. They are helping to build up their airline, which they have not a token part of but a real part of.

Mr. Kolter. So, in other words, you are indicating that your plan will mean that if there are wage concessions they are agreed to, and we will not have this confrontation?

Mr. Ritchie. That is right.

Mr. Kolter. Well, I want to thank you for your answer——

Mr. Ritchie. They have already agreed to them. They have already agreed to concessions far beyond anything that was being, what was being negotiated before, and furthermore, they have agreed that for the future, should any of these problems ever arise again, they are happy to have some neutral third party arbitrate it on the basis of what is fair, instead of on the basis of the power and leverage each party can bring to bear.

The unions have even agreed that they will allow the noncontract people to receive their piece of the pie on the same basis, something which there is no self-interest in granting.

But it is because they believe it is right, and they are happy to go forward on the basis of an agreement that they simply believe is fair and will give them a fair shake.

I think there is a lot more workers like that in this country than most people think, by the way.

Mr. **Kolter.** Mr. Ritchie, I am thoroughly delighted by your answer. Thank you very kindly.

[Laughter and applause.]

Mr. **Ritchie.** I am delighted to give it.

Mr. **Oberstar.** Mr. Molinari.

Mr. **Molinari.** My recollection is that when Eastern was operating before the strike, they were showing a loss of approximately $1 million a day. Obviously since the time of the strike Eastern has lost a lot of its business to the competitors.

You mentioned that before, in your opening statements. Assuming that the Ritchie offer was approved and accepted, I think it is fair to say you are going to start operating at a loss. Would you agree with that? I see Mr. Carlucci saying yes.

Could you give us an estimate. I am looking at an offer of $100 million in cash plus give-backs. What kind of a loss are you anticipating and when would you reach the point where you might be in the black?

In other words, I am trying to see how you jump the gap from that $100 million. I can see that being eaten up in a relatively short period of time. How do you survive?

Mr. **Holt.** Congressman, my name is Paul Holt from Cambridge International Partners, financial advisors to Mr. Ritchie.

Our plan contemplates that there will be significant cash operating losses incurred in ramping up the airline over the first 5 to 6 months that——

Mr. **Molinari.** Can you estimate what those significant losses might amount to.

Mr. **Holt.** Those cash-operating losses are likely to be of the order of $200 million, when taking into account the exceptional expenses that will be incurred in bringing the company out of bankruptcy. Approximately $50 million of that amount relates to the specific expenses of the bankruptcy administration that will have to be settled before a plan of reorganization is consummated, and those amounts are allowed for in the financial projections which are embraced in the Ritchie plan.

Furthermore, we would contemplate that in the first full year of operation, post ramp-up, that is, in 1990, the airline would be profitable, substantially profitable on an operating basis, and generating cash with which to meet its debt service.

Mr. **Molinari.** Is your company, or any of the other companies here, willing to invest some of your own money in this venture, in the Ritchie proposal? Or are you here merely as consultants?

Mr. **Holt.** Our company is an advisor to Mr. Ritchie, and are not ourselves investors.

Mr. **Molinari.** Is there anybody out there that says they are willing to offer some financing to the Ritchie proposal as you go down the line? I am trying to see what happens after that $100 million is expended. Where does the rest of that money come from to keep you in business?

Mr. **Harris.** Well, we have, today, $100 million, and I believe more than $100 million of capital committed to get the airline started. We will have to raise more money through that process.

Mr. **Molinari.** Excuse me. Through what process?

Mr. **Harris**. Through the bankruptcy process as the airline is ramped back up. We believe that can be done through financing, provided there is an agreed-upon plan and a consensual transaction between the buyer and the seller.

I do not believe you can raise capital unless you have a consensual transaction, because there will be potential litigation down the line. Whether you confirm a plan or consummate a plan, you still have a legal process that could hold the airline captive for a while, as litigation proceeds between the former shareholder and the new shareholder.

So you have to have a consensual plan. Then I believe you can raise the capital. We have $100 million of capital today, $125 million. We will need to raise more, but I believe we can do that.

Mr. **Ritchie**. Mr. Molinari, can I address the other facet that sounded implied in your question, which was, is anybody else out there as crazy as Joe Ritchie and willing to put money into this thing? And I think it is a good question because whatever my business experience might have been—maybe I was lucky.

The answer to your question is—well, or maybe crazy. I have approached a half a dozen other businessmen, not professors of economics, not folks from Tibet or from the bay area, with garlands in their hair. Not consultants, not advisors. And they are all people who have made their own personal fortunes, starting from scratch.

So far, my batting average is a 100 percent. In each case, they have said, based on the approach we are taking, they would put some of their own capital in, and none of the amounts was under $1 million.

So there are other people who have made money, taking business opinions, that feel as I do.

Mr. **Molinari**. We are running out of time before a vote. Can you give me an idea as to what those various offers might add up to?

Mr. **Ritchie**. That is part of the original 100 that goes in and it would be some place between $30 million and $50 million going into the bankruptcy, understand, and that is why it is so high risk. To my knowledge, it has never been done before.

Mr. **Molinari**. I see my time is up.

Mr. **Harris**. I would just point out——

Mr. **Molinari**. I am sorry. Please.

Mr. **Harris**. I just wanted to point out that under our plan, we have already committed $100 of new capital to go into the airline.

It is my understanding that the Texas Air proposal has no new capital. Now I have not seen that plan, but my understanding is there is no new capital going into the airline under that proposal.

Mr. **Oberstar**. The committee will stand in recess pending the vote on the House Floor now and resume in about 15 minutes at which time the gentleman from the Virgin Islands, Mr. de Lugo, will be recognized.

[Recess.]

Mr. **Oberstar**. The committee will come to order. At the time of the break, the Chair recognized the gentleman from the Virgin Islands, Mr. de Lugo, who is now ready to begin.

Mr. **de Lugo**. Thank you very much, Mr. Chairman, and I want to commend this panel, Secretary Carlucci and Mr. Ritchie, for their presentation here today. It has been very helpful to me, and I am sure it has been very helpful to this committee, and to this entire process.

I think what we are hearing is that beyond the Eastern problem, which has been so eloquently stated today by the members who appeared here, and by this panel—the whole question of the way deregulation is working—that this is not the way we all hoped it would work.

We all thought that deregulation would mean more competition, not less, and there are whole new areas that have evolved with deregulation, that did not exist a few years ago. The hubs that were alluded to earlier. The term, "critical mass". I do not know if that even existed a few years ago. Critical mass. The thing that really bothers me about this whole problem with Eastern is that we have under one umbrella Texas Air. Two competing airlines.

We have an airline that has a proud history. I mean, when you talk about the airline industry in this country, you talk about Pan Am, you talk about Eastern, you talk about United, and one or two others. Those were the giants—the pioneers, the giants—and we have a company here, in Eastern, with loyal employees committed to the success of this airline, dedicated to it, and what we have is people coming into the airline industry who are businessmen, with no particular history, perhaps, in the airline industry. They are coming in and looking only at the bottom dollar.

Now, we are fortunate in this case, that Mr. Ritchie, who does not have a long history in the airline industry, comes in with a philosophy that I could only hope would be applied by more companies.

But my problem, with what I have heard today, is when we talk about selling off the Miami hub, and selling off the Latin American and Caribbean routes—are we doing this to strengthen Eastern or are we doing this to liquidate Eastern?

I would like to ask: Is there anything that would stop Mr. Lorenzo from selling the Miami hub and these routes to Continental, for instance? Is there any legal prohibition to that? Or is that simply stopped because of the situation we find ourselves in today? Mr. Thayer.

Mr. **Thayer**. If I may answer that, sir. I do not think there is anything to stop him. I think what stopped him, at the moment, on South America, is Secretary Skinner's comments about you may not be able to just sell these routes, like was done in the past.

The other thing is, I think that has probably stopped him, is I am sure there are a number of bidders out there and some of them are uncertain about those comments, and also are trying to see at what value they can get them.

I think these valuable assets that are on the docket to be sold are literally the "swing" in what I view as my correct professional analysis of this. The "swing" in losing that critical mass. And you are so right in your comments, that before deregulation you did not need critical mass, and I can very easily explain why.

You had a route franchise that very little competitors were allowed to operate on, and so critical mass was not necessary. You got traffic from other airlines. For example, in Braniff, which I headed for a number of years, 50 percent of your traffic was interlined from other carriers.

When deregulation came along, that went away. So the airline that had the small system, like the regionals, it was no accident that a National, a Braniff, a Continental, and a Western are gone. They lost their interline feed and they were not able, for their size, and the size of their pockets, to get to the hubs as effectively as the others, and that is why the word is new in deregulation. Now they gather their own traffic and it comes over their hubs, and that is the purpose of them. So you are very right, sir. Very right.

Mr. DE LUGO. Thank you, Mr. Thayer. I see my time is up, Mr. Chairman.

Mr. OBERSTAR. The gentleman's time has expired. The gentleman from North Carolina.

[No response.]

Mr. OBERSTAR. The gentleman from Missouri. Mr. Hancock.

Mr. HANCOCK. Thank you, Mr. Chairman. Mr. Ritchie, as a businessman considering buying, or attempting to buy an operation that has consistently lost money—I am sure you have analyzed the background and the history of these losses—has Eastern's situation evolved from mismanagement, from excessive interest costs, or, I mean major factors? Or is it a lot of little things that have entered into it, that you figure you can straighten out within the operation of Eastern and put it back on a profitable basis?

Mr. RITCHIE. I could not hear all the question, but it sounds like you are asking what I think the problem has been in the past?

Mr. HANCOCK. Yes. Is it major problems, major decisions, mismanagement, mis-use of corporate funds, excessive interest costs? You know, we did go through a period of pretty high interest rates.

Mr. RITCHIE. Yes.

Mr. HANCOCK. Or is it a lot of little things within the operation of the airline?

Mr. RITCHIE. Good question. In any of these situations, I think you can look at it and see a lot of little things, but I think they are symptomatic of one big thing, and that big thing is how you relate to the people who do the work.

Eastern used to make money years ago. It has done badly, recently. If you get that wrong, everything else has a way of "going to hell in a handbasket" in a big hurry, and that is what I think has happened at Eastern.

As we have looked at airlines, one of the first questions when you are looking at a business is, what do you bring to the table and how important is that thing you bring? Well, let's suppose that what you bring is that you understand human beings, the stuff we all learned at our mother's knee, but which you do not learn in Harvard Business School.

Now, if that is what you bring, then you had better ask, okay, how important is that to this industry? I was amazed to find out how important it is to the airline industry. I would not have thought that before I saw it. It is tremendously important.

You take your business plan and make one little change to productivity, or to the load factor which comes from the atmosphere you have, and so on, and the numbers on the bottom line go through the roof or drop through the floor. So very little things like that make a huge difference.

But I think fundamentally, all these things are symptoms of people not simply relating to people the way we learned as children you should relate, and so I have tried not to misstate what I think are symptoms for causes. I think that is the cause. It is why, when I looked at this, I started out by talking to the people that worked there, rather than starting out by looking at business plans or talking to financial analysts.

You have to get to that, and I think we have spent more on that than anybody, but you have got to start in the right place. So that is where we started.

Mr. HANCOCK. I have not, you know, looked at the detailed parts of your plan, but have you considered employee participation other than through the airline pilots pension? In other words, stock ownership programs, or ESOPs, and this type of thing, in your bid for it?

Mr. RITCHIE. The particulars we have looked at a lot, yes. The main point is you have got to want to. When you get that right, then you have all kinds of tax consequences of different methods, and so on, and you have to sort through all that. But if you are doing it from the top, as a bargaining position, as something that they are making you do, then I think it is doomed to failure.

If you are doing it because you want to do it, because it feels better to have the man in the machine shop trying to get that plane fixed on time, be your partner rather than your employee, then all that other stuff just seems to take care of itself.

Mr. HANCOCK. But you do not preclude that at all——

Mr. RITCHIE. Pardon?

Mr. HANCOCK. You do not preclude that at all as a future objective?

Mr. RITCHIE. You mean other means of participation?

Mr. HANCOCK. I mean if in fact you were successful, you would not preclude an employee stock ownership involvement in the future?

Mr. RITCHIE. Not at all. We are looking at it and we are doing it now.

Mr. HANCOCK. Thank you, Mr. Chairman.

Mr. OBERSTAR. I thank the gentleman. Mr. Laughlin.

Mr. LAUGHLIN. Thank you, Mr. Chairman. Mr. Thayer, I certainly concur in one of your observations about events before deregulation. You did not say it, but I am sure you are implying the customer or the traveling public certainly got far better treatment prior to deregulation.

I listened to your example. My first experience in coming to Washington, D.C. as a young Army reserve officer from the Houston area, you had to fly through Atlanta, and you could call either Eastern or Delta to get to Atlanta, and more times than not, you would fly on the other airline from Atlanta to here, and it was always at the passenger's convenience.

Now with this hub system, and some of the other gimmicks that they have, the person that decides that they have to make a trip often pays double of what the person who is the infrequent flyer, that goes to the airport. I have a real problem with who has got the traveling public's best interest in mind these days—but that is not exactly the reason we are here—but I wanted you to know that I shared some of the thoughts you were expressing.

It may be better for you, or Mr. Ritchie to answer this question, but is there a point at which your plan ceases to be workable if Eastern is permitted to continue to sell off the assets that I, as one, who have no airline experience, but in sitting on this committee for the last six months I have heard about the sale of the Eastern shuttle, the computer system, hubs, landing rights, the Caribbean routes.

Is there some point at which those assets cease to be part of the Eastern organization you are trying to purchase, at which your program is not workable and is just thrown in the garbage can and walked away from?

Mr. **Thayer**. I think we are right at that point right now, and that is why I raised, so strongly, the assets that are still left. In other words, some of the assets that have gone so far have not been that critical.

In my analysis, from here on, they get very critical because they start talking about gates, they start talking about slots, they start talking about route authorities, and they start talking about gateways. These are all the "skin and bones" and the "muscles" of an airline. And from here on, it is very critical.

Mr. **Laughlin**. Well, what can be done to salvage this tragic, unfortunate circumstance that we are all gathered here today to listen to?

Mr. **Thayer**. I do not know whether I can answer that question.

Mr. **Ritchie**. What can be done to what, Mr. Laughlin?

Mr. **Laughlin**. Salvage. So that we have a valuable entity, that either the Ritchie plan, or someone is interested in making into a profitable airline. Is there anything that can be done?

Mr. **Ritchie**. Well, we think the asset sales have to be stopped until it is sorted out. It is a low-cost thing to do, and it gives the chance of looking at it long enough to determine whether or not it is actually viable at the small level. We think just inspection of the facts will yield the right answer.

Mr. **Laughlin**. Mr. Thayer, I do not know what your time of service was with Braniff, but you certainly had—and I do not need to know—but you had, certainly, a familiarization with the demise of Braniff as a major carrier. What is different about Eastern, that gives you and the group you are associated with today, any hope or expectation that Eastern can be brought back from the "death bed"?

Mr. **Thayer**. I think there are two very different circumstances. Eastern is a major carrier in size, and the question I have is in down-sizing it to the degree that I think they are planning to do with the asset sales will put it in an untenable position in the very intense market competition that is out there now.

The experience in Braniff was trying to go the other way, from a small carrier, which the regionals were, up to be a major carrier in that period. So my intense concern is if you go the other way down, in a deregulated economy, in a deregulated airline industry, you are doing the wrong thing. You are doing the wrong thing.

Let me give you just another example. The smaller ones that are still successful, and still out there, like Midway and America West, are desperately trying to grow faster, get more muscle, get more critical mass. That is why they participated in trying to get the Philadelphia gates and the airplanes connected to that, to build their critical mass.

So going the other way is just the wrong thing to do in the forces that are in the marketplace today.

Mr. **Laughlin**. If timing in this situation is so critical, is anyone bringing this to the attention of the bankruptcy judge, and, if so, are we interfering with that process in any way, in the hearing we are having today?

It seems to me that all this is pending in the bankruptcy court, and that is where some of the decisions, or the major decisions have to be made. Is that judge aware of the critical timing involved?

Mr. **Seidel**. You are quite right. These are matters that are properly brought before the bankruptcy judge's attention. The Ritchie group is not a party that can speak there. The unions are very much interested in bringing this particular matter to the bankruptcy judge's attention.

Judge Lifland has chosen to ignore it, and allow asset sales to go forward. The bankruptcy code permits asset sales out of the ordinary course of business with bankruptcy court approval. There is an issue, however, whether or not the bankruptcy judge could approve asset sales if it were a sale of substantially all of the assets of the debtor, outside of what we call the "plan of reorganization".

What we face in Eastern Air Lines is what has been referred to as a "creeping" sale of all the assets. They have gone in, and on an item by item basis, have been able to convince Judge Lifland that it is not a complete sale of the assets.

But if you took a snapshot, probably two months from now, and could look back to where you were when you started the proceeding, one would probably say this was a sale of substantially all of the assets.

I do not know what more we can do to prevent Judge Lifland from authorizing those sales. I would suspect that one thing that might be asked—and I am hesitant to go further because it probably reveals strategies that probably should not be brought before your attention—but I suspect that if one could prevail upon Judge Lifland, as Mr. Ritchie has said, to not consider any further sales pending an examination of the filed plan of reorganization in this case, that would be better for everyone.

The judge could consider the public interest involved there, and we could make a more informed decision.

Mr. **Oberstar**. The gentleman's time has expired. The Chair recognizes the gentleman from Minnesota. Mr. Stangeland.

[No response.]

Mr. **Oberstar**. The gentleman from Ohio. Mr. McEwen.

Mr. **McEwen**. Thank you, Mr. Chairman. I thank you gentlemen for coming today. I just have about three quick questions to try to piece this together. What do you estimate to be the asset value of Eastern, presently?

Mr. **Harris**. The total assets of Eastern, including those assets not on the balance sheet, such as some of the gates and slots. We have estimated, we have appraised those asset values I believe something on the order of—I want to be sure on this. Can I ask one of my associates to produce that information.

Mr. McEwen. Surely.

[Pause.]

Mr. **Harris**. Congressman, we have gone through an evaluation of the asset values of Eastern, using their balance sheet as of 3-31-89. The total assets on the balance sheet, at that time, was approximately $3 billion, excluding the capitalized leases which of course is equipment that Eastern does not own.

We did what we think is an optimistic asset-sale scenario, and those assets we believe would produce $4.3 billion in that scenario, and that is allowing for some of the higher-than-appraised asset sales that have been taking place so far to date.

We then did a pessimistic liquidation scenario which would basically involve the sale of assets under a very short time frame, and, as you may know, many of these assets are special-type assets which only can fly on certain configurations and certain routes.

Therefore, you might not find a buyer as quickly as you would like, and have to lower your price. We think, on a pessimistic basis, those assets could be sold for $3.6 billion.

So the range of values that we would suggest is applicable in a liquidation here range from $4.3 billion to $3.6 billion.

Mr. McEwen. And what is the present debt?

Mr. **Harris**. The present debt, as per the balance sheet date of 3-31-89, was approximately $3.6 billion. Now that excludes certain claims against the operating leases, the capitalized leases, I should say, and it does not include certain claims that could arise through the termination of the pension plans, and health-care claims that certain employees may be entitled to in Eastern.

Mr. McEwen. So the debt would be a low of the balance sheet debt of 3.6 and could go as high as what?

Mr. **Harris**. 4.3.

Mr. McEwen. 4.3. And you would anticipate additional debt of how much in this proposal here?

Mr. **Harris**. In the proposal we are looking at, we believe there would be additional debt of somewhere around $270 million.

Mr. McEwen. I just would have a question. In politics, people ask you tough questions all the time. You cannot take them personally. There was a company that many of us felt very dear to. It was sold in 1986, to someone whose parent has picked up additional assets, and the purchaser is now selling them off, will have cash at the end, and the airline will be gone. I think that is basically, all steps aside, the bottom line.

What is there to convince a 20-year Eastern employee that that is not about to happen again with the new owner?

Mr. **Harris**. Well, as the plan now sits, the employees will in effect become the owners. Now we have been told—and let me specifically reference your question about the new debt, because this ties in, I think, to a very key question, which is where is the new money, where is the new capital?

Well, we have said there is $100 million coming in, which upon completion of the ramp-up would convert to equity. Now there is another $50 million that has been more or less committed to by the AFL–CIO.

And then people say, well, there is still not enough capital in this. Well, when I learned economics, I learned that the most fundamental capital a person could contribute was their labor, and what the employees of Eastern, the new owners, if you will, have offered to do, is basically support the airline to the extent of $170 million in wage concessions for 5 years.

They have offered to give up additional wages through the ramp-up period, that could total another $150 million. And there are significant proposals under consideration to eliminate work rules, readjust scheduling, increase the flying time. These are the most fundamental kinds of capital one can contribute, and they should not be denigrated and they should not be ignored.

All of those serve to make the Ritchie proposal and the reorganization of Eastern much more feasible.

Now, there will have to be capital brought in to either repay creditors or repay the equity, but that can be done.

Mr. Oberstar. The gentleman's time has expired. But continuing on that point, what will be the annual cost of carrying that debt, to take that point a little further? It is a matter that we have been reviewing with the Northwest Airlines acquisition. It is a matter that has been of concern in other airline acquisition issues.

Mr. Harris. Well, in terms of the cash——

Mr. Oberstar. Very briefly.

Mr. Harris. Again, if you look at basic rates today, between 12 and 13 percent. So somewhere between $25 million and $30 million. Now when we go to the market, rates can change.

Mr. Oberstar. Is that the cost of carrying new debt and current debt?

Mr. Harris. No. The current debt burden would total about $270 million.

Mr. Oberstar. Thank you. The gentleman from California. Mr. Bosco.

Mr. Bosco. Thank you, Mr. Chairman. In looking out over the room today, I cannot help but have a sense of "deja vu". In 1981, in the California legislature, we had a meeting very similar to this, a lot of pilots and stewardesses, and others, whose lives and families were in jeopardy at the time. At the point, the very beginning of the deregulated environment, Frank Lorenzo was going to buy Continental Airlines, and the employees, at the same time, had a proposal to buy it and they had their financing, and it literally was a battle similar to this one. And at that time I was sitting on the Ways and Means Committee in the California legislature, and I asked the representatives of Texas Air a couple questions that we were very concerned about in California.

First of all, are you going to lay off any people? Because his was a California corporation. Second, were you going to move the airline out of California? And third, were you going to raid the assets of Continental to destabilize it and harm its ability to operate profitably?

Mr. Lorenzo informed us—and I have a copy of the letter in my files—that no, the employees were not going to be laid off; no, the airline was not going to be moved from California; and no, there was no intention of raiding the assets.

Within a period of months, all three of those things happened. For that reason, I have to beg the indulgence of the Chair, but I cannot look at this issue entirely objectively.

This same group I think has been fibbing its way across the business landscape of this country for the last decade, and are here today in very much the same situation. The same people, the same families destroyed. Interestingly, they have not made a profit, either. They have operated what the Wall Street Journal calls the "sickest airlines in the country", and I do not know what Judge Lifland's considerations are—and I know him to be a good jurist—but I certainly hope he takes these things into consideration.

But Mr. Ritchie, what happens when the cheering stops? What happens when the pilots go back to work, and the flight attendants, and others, and you own the airline and then your first big dispute comes up?

I mean, I can understand now, where people would have a feeling of solidarity. But is there something built into your plan, inherently, that is going to put you in any different position later on than Mr. Lorenzo is in now? When "push comes to shove," when people start to say, well, I do need more money, or I have taken too many concessions, and my kids do need to go to college, how are you going to be in any different position than Frank Lorenzo is?

Mr. Ritchie. Well, the first part of my answer to that question is that when you treat people differently they behave differently. I have been in many partnerships. I have done them on the basis of good faith. I just have not had that kind of problem.

But I do not expect other people to believe that, and so we have agreed on how these problems are going to be solved down the road, absent the ability of our good faith to solve them.

And the agreements are that since we all maintain—and I believe sincerely, that we want these things to be done in good faith, and fairly—everyone is willing to submit to fair arbitration rather than quarrel their way through it. This is granted even by people that have no economic incentive because they have much more power if they were to solve the problem merely by power, and it is agreed to that disputes between unions, between union and noncontracts, between union or labor types of people and myself—all would be done this way.

And it is agreed to, happily. This is not a concession that has been extracted from these people.

Mr. Bosco. May I ask for what period of time this would be?

Mr. Ritchie. This would go on, indefinitely.

Mr. Bosco. But this would be a contractual agreement, not just a handshake?

Mr. Ritchie. Yes. It would be contractual.

Mr. Bosco. In other words, you would be able to guarantee that there will be no strikes, and an arbitration system would have been agreed to by management and labor? Is that accurate?

Mr. Ritchie. Well, I am not interested in owning this airline without that kind of understanding, and we have discussed that thoroughly with all unions, and everybody understands it.

Mr. Bosco. And that is the agreement that you have reached?

Mr. Ritchie. That is what we have agreed to. Yes.

Mr. Bosco. Thank you.

Mr. Oberstar. Mr. Ritchie, what is there in your proposal that would make Mr. Lorenzo step forward and accept it? What does he get out of it? What is his financial recompense that is attractive to him, as the debtor-in-possession, that would say, "It's a deal"?

Mr. Ritchie. The proposal we originally made, which is in the ball park with the new one we are making, offered $200 million in preferred stock, roughly $250 million in other types of intercompany forgivenesses, along with some other things which Jim Harris could detail.

But when you ask the question the way you did—what is there that would make him step forward and do the deal?—that is a different question and I have no idea how to answer that question.

We have been told that the minimum that would be acceptable would be $500 million cash, up front, in the bankruptcy, in addition to a lot of other things, which bring the total closer to a billion.

And so we have a problem with closing the gap. The offer we made we believe was substantially above fair value, and perhaps to clarify this point—which I think is a very big point—I might as well tell you the position we have taken privately, but I guess which now has become public anyway, and which has been reflected in a letter to Mr. Lorenzo which I will read a few sentences from because I think it clarifies the point.

> Unfortunately, we've still not met to discuss my interest in acquiring Eastern, which process I am continuing to work on through the proper process. I am very concerned about establishing a sensible dialogue with you about fair value and a consensual transaction. To this end, I would even consider spending up to a million dollars to move forward evaluation discussion, as will be explained later.
>
> I feel that I must write you in an attempt to find a way of better establishing value of Eastern as this seems to me to be the issue at the heart of the current dilemma. It is also the issue affecting the lives of many Eastern workers, your companies, and all financial parties involved.
>
> At the Houston meeting we discussed getting Shearson and your staff together to discuss, in detail, the differences between us regarding value. Bob rejected this idea, but I would still be supportive of this discussion if it could be arranged.
>
> Somehow, we must find a solution to this value dilemma. I feel there might be a way of using an independent third party to identify a narrower range of value to help bring us together. For my part, I would be happy to have you identify a fair third party who could establish a fair process of determining current value to the equity holder, using an independent professional group.
>
> I would even cover the reasonable cost of this process, up to a million dollars, on the condition that all necessary information was made available to the selected professional group and that if the final value is closer to my professional's value of zero, than yours of over one billion, you would then refund the costs, not to me but as payment to a recognized charity selected by me.
>
> I will bear this cost as I really want to find a sensible way to resolve the current impasse. Assuming a fair value could be identified, I would of course realize your expectation to receive an amount substantially in excess of this value.

That is the position we take. We recognize there are disputes in this, where we differ by light years. All we can do is offer to have a neutral third party look at them.

Mr. Oberstar. That may be an option that the examiner will address. We will get to that point when he presents his views. But my understanding is that the examiner proposed that you make an offer to Mr. Lorenzo at least as favorable as the Ueberroth offer.

Is this your offer? Is this letter your response to the hearing examiner?

Mr. Ritchie. Let me take a minute to compare our offer to the Ueberroth offer. We actually think it is a much better offer. I have told the examiner, I will make the Ueberroth offer every day of the week. The Ueberroth offer risks no capital. I would much rather risk nothing than risk a large hunk of my own net worth, and if the plan does not work, Mr. Ueberroth could walk away from the transaction with $20 million. That is the other part that I would much rather do than risk a hunk of my own net worth.

So, that is an offer I would make any day, if all I am interested in is personal gain. The offer that we are making, we put our own money out and we cannot walk away. We take the risk of the ramp-up. We take the risk of the whole thing working.

So, in that sense, the Ueberroth offer really offers nothing from Mr. Ueberroth's standpoint because he does not put money at risk in the bankruptcy.

Now, the other problem is this: That the Ueberroth offer, while it puts a lot out for Texas Air, puts out so much that in our opinion the airline becomes totally unflyable. As has been pointed out by a number of people here, there is a question of whether or not it can fly anyway, but there is no way that it can take $460 million of cash and hard assets, throw them out the window and then fly.

So the Ueberroth offer is viewed as one that could not have had acceptance by the creditors committee in any case. In fact, Mr. Shapiro has asked us to make that offer not because it is a flyable airline under that scenario, but as a tactic to bring Mr. Lorenzo to the bargaining table.

In our view, we simply cannot negotiate in that way, putting things out on the table that we honestly believe are not workable just as a part of a ploy to pull somebody into a negotiation, and furthermore, we have no assurance that Mr. Lorenzo would not accept the offer, leaving us with a totally unflyable airline.

Mr. Oberstar. I would like to follow up on that but at this poin I want to defer to the gentleman from Georgia, Mr. Lewis, who ha not had an opportunity to ask questions.

Mr. Lewis. Thank you very much, Mr. Chairman.

Mr. Oberstar. And I would note that we are on the second cal of a vote.

Mr. Lewis. Mr. Chairman, I do not have a question, but I woul like to take the opportunity to commend Mr. Ritchie for hi moving testimony. I think he is a living witness to the fact tha you can be a very successful businessman, and, at the same time have a sense of sharing and a sense of caring. I really appreciat that. Thank you.

Mr. Oberstar. I thank the gentleman for those remarks. I wan to thank this panel for your responses. We will recess for 10 min utes, 15 minutes, depending on how long it takes to vote, an resume with our next witness, Mr. David T. Shapiro, who is th court-appointed examiner in the Eastern Air Lines bankruptc case.

Mr. Ritchie. Mr. Chairman.

Mr. **Oberstar.** Yes, Mr. Ritchie?

Mr. **Ritchie.** Can I make one closing remark? Can I make one closing remark because a couple of questions were raised in the last couple that——

Mr. **Oberstar.** In one minute.

Mr. **Ritchie.** Okay. One minute. The issue of whether or not what we are doing is not really just serving to prolong the strike, that it is not real, that it cannot fly, and so on. Believe me, that is the last thing I would want to do with these people who are out on strike, and accordingly, we have made the offer to have an objective third party look at our plan. If it is not flyable, we will be happy to go away.

You could have the Department of Transportation look at it. You can have your own experts look at it. It has been said that it has already been looked at by a neutral third party.

Yes, it has been looked at by a number of them, and one opinion of one of them has been picked out, and if you would like to have those who have already looked at it be the panel, that is fine, too. We will look at it either way because we believe it stands up under scrutiny, and I simply offer this in good faith as a means to solve this logjam.

Mr. **Oberstar.** I thank you very much and it is important to have that point on the record. You did say that in 58 seconds. [Laughter.]

But the response, and the whole point of this hearing raises some very serious questions about the adequacy of current law to cover this very complex airline business. The tools available to the Department of Transportation, in my judgment, after years of reviewing them, are inadequate. They are blunt instruments. They do not allow for fine-tuning, and the bankruptcy law does not seem to have the kind of flexibility needed to deal with this situation.

That is why I think we have Mr. Shapiro here, to fill the gaps in knowledge about this very, very important airline and public policy issue.

We stand in recess for roughly 15 minutes.

[Recess.]

[Mr. Ritchie's prepared statement follows:]

HEARING BEFORE THE SUBCOMMITTEE ON AVIATION
HOUSE COMMITTEE ON PUBLIC WORKS AND TRANSPORTATION

TESTIMONY OF JOSEPH J. RITCHIE

Mr. Chairman and Members of the Aviation Subcommittee:

My name is Joseph Ritchie. I am a Chicago businessman as well as being President of Chicago Research & Trading Group, Ltd., one of the largest traders of futures and options in the world. More relevant here is my interest in purchasing Eastern Air Lines in partnership with its employees.

I appreciate your invitation to appear before you today because, quite frankly, this hearing provides me with an opportunity to present my views on the future for Eastern. My purpose in testifying is to state my case: about my views on labor-management relations, about what I found at Eastern, about observations relevant to the public interest, and most importantly, about what I believe Eastern can be once again.

Although it might not be obvious from those I have been working with these past few months, I am a conservative from the Midwest. I am firmly a capitalist in the classical meaning of that philosophy. I believe that workers ought to be compensated according to their overall contribution to the business which includes not only their productivity but also their attitude and loyalty.

But therein lies the rub, as well. Too often compensation is not determined by these factors, but rather by the respective bargaining power of labor and management. This unfortunate reality creates mistrust and fosters an adversarial relationship between labor and management. It also contains an inherent conflict of interest. Each side fears that cooperative behavior will simply be exploited by the other. The relations between labor and management thus can become enmeshed in the seamless web of power, antagonism and exploitation.

I reject that prescription for disaster, although it is the way many companies are run. I believe that true fairness and cooperation begets fairness and cooperation in exchange. Labor must acknowledge the risk of failure as well as insist upon a share of the fruits of success. Management equally must recognize the contributions of, and the objectives they snare with, labor.

I have applied this philosophy to my businesses, with what I believe to be great success. If I have ever seen a group and situation ripe for this approach, moreover, it is the Eastern work force.

Twelve years ago, I founded the Chicago Research & Trading Group with three partners. Our firm has grown from the four founders in a single Chicago office to a global business with offices in Chicago, New York, Philadelphia, San Francisco, London and Tokyo.

Throughout this growth cycle, we have sought to maintain our fundamental principles. We allowed those experts in a field to act as team leaders regardless of seniority. I determine my partner's compensation, but they determine mine. Like any organization, we have had our share of problems; however, at the bottom line, our system works. I am far prouder of the team we have built, and how well they work together, than of our financial success. Those two things, together, enable CRT to accomplish with a relatively small group, what other Wall Street giants find difficult to do with large numbers of people.

This same philosophy is what attracted me to Eastern. Even from afar, I could sense enormous pent-up productivity that could be unleashed if rancor could be supplanted by trust in the relationship between labor and management. I became even more convinced of this potential as I came closer to this situation and met many of the key union players involved. The more closely I worked with both leaders and the rank and file of Eastern's workforce (first machinists, then pilots, flight attendants and non-contract employees), the more I became convinced that Eastern enjoyed human assets of untold value, which are now just being wasted. Most workforces lack a taste for this kind of approach, or are not ready for it; but if ever there was a workforce that is ready, Eastern's is it.

The letters that have come to my family and me during the past several days from the people of Eastern have been deeply moving. What heart and soul the letters have! These writers repeat over and over and over again that they are not talking pay: they are talking pride, integrity, respect and dignity.

Working in concert with Eastern's union works. I believe that our team has created something special. Our plan is a prescription for success. This substantially recapitalizes the airline with new risk capital, satisfies the creditors in full, enjoys the support of Eastern's workers and is accompanied by a detailed business plan that realistically outlines the restoration of Eastern to a stable base from which it can continue as a major competitor in the airline industry.

Our offer and its associated business plan include the following:

1. Substantial new capital of up to $350 million. Of that total, $100 million would be placed at risk in Eastern during bankruptcy to support the initial ramp-up process, which involves the re-establishment of normal flight operations. The balance would be invested as Eastern emerges from bankruptcy. Of this capital, $75 million of the initial $100 million is underwritten by:

	$ Millions
Joseph Ritchie	25
ALPA, IAM	25
ALPA-B Pension Plan	25
To be placed	25
	$100 Million

2. Major voluntary wage concessions from the union workforce involving:

a) A 20 percent wage concession for 5 years, or $210 million annually based on the pre-strike work force level. On a prorata basis, this concession approximates $170 million a year for 5 years. (Total $850 million).

b) Further wage concessions underwriting cost savings or revenue improvements up to 2.5 percent per annum. (Total $280 Million).

c) During the six-month ramp-up period, an additional wage support program, ideally including all

Eastern employees, of 35 percent of wages to be available to cover excess net costs above pre-agreed business plan levels. (Total $175 Million).

3. Based on these commitments, assuming prudent due diligence and Eastern's emergence from bankruptcy as planned, the balance of equity and debt financing totaling over $450 million would be arranged and provided through Shearson, Lehman, Hutton, Inc.

4. Prior to any final commitment for the post-bankruptcy financing, the providers of equity and debt would require comfort that a consensual transaction is possible and that proper financial procedures would be followed.

Even now the Ritchie plan involves substantial risk capital injections and already agreed 5-year wage concessions to support a going concern. Voluntary wage concessions or alternative benefits will exceed $1.3 billion over 5 years.

In addition to this substantial financial commitment, available today, further equity and debt commitments also would be finalized to reach a consensual transaction. In this process, all creditor claims would be satisfied.

The above commitments were incorporated in a 202 aircraft business plan as part of a $450 million offer to

Texas Air Corporation. That offer was subsequently rejected as totally unsatisfactory. Based on the latest court-approved aircraft sales, we have reworked our business plan at a level of 196 aircraft. We believe this plan is viable, including all the capital and labor concessions incorporated into our rejected offer.

We have commenced preliminary discussions with the professional advisors to the Creditors Committee concerning our current plan. I have also communicated with Mr. Lorenzo in an attempt to explore ways for us to discuss further our differences of opinion and to possibly find a consensual solution.

Jim Harris, of my financial advisors, Shearson, Lehman, Hutton, together with Paul Holt of Cambridge International Partners and Russell Thayer of Airline Economics, Inc., are available to help me respond to any specific questions you might have about our business plan to the extent permitted by confidentiality agreements.

When I became involved with Eastern, I saw a massive human problem coupled with a very serious business situation. I believed then, and still do, that with common sense, the right approach to dealing with people, and continued effort, it is possible to preserve Eastern Air Lines as an effective competitor. We are involved in a very complex, confusing and emotional transaction, and I have been fortunate to have qualified and highly professional advisors working with me. We believe that we have found a sensible way to overcome most of the hurdles, or at least to see a realistic way of doing so. Unfortunately, we now may be close to the point at which Eastern ceases to be a competitor and becomes an unattractive commercial opportunity: as the aircraft fleet is depleted by continued asset sales, the future viability of Eastern becomes further impaired, while a consensual agreement with Texas Air Corporation continues to elude us.

I continue to be optimistic that common sense can prevail, and I will continue to make reasonable efforts on this premise. However, facing continuing asset disposals, particularly proposed additional aircraft sales, I have serious concerns regarding the future survival of Eastern as a major independent competitor in its industry and as a reasonable commercial investment opportunity.

Thank you for the opportunity to testify here today. I will be glad to respond to any questions that you might have.

Mr. Oberstar. The subcommittee will please come to order.

Our next witness is Mr. David T. Shapiro, who is the court-appointed examiner in the Eastern Air Lines bankruptcy case.

Mr. Shapiro, we greatly appreciate your participation in this hearing. I made it clear, at the outset, that the purpose is not to advance one or another proposal in the course of this hearing, but to understand where the process stands, and we also want to make it very clear that our purpose is not to influence, one way or another, the bankruptcy court, but to get a sense from that branch of where the bankruptcy proceeding stands, and how it affects the future of Eastern as a participant in the airline industry.

This is a very important public policy question. I think the role of bankruptcy proceedings is not well understood generally by the public, and I must say, by members of our committee, particularly as it affects this unique case.

So I look forward to your testimony to enlighten us, and I also want to point out to our colleagues that there may be some questions asked, that may be of great importance, to which the answers may be privileged information, and of course under your obligation and role as examiner, you will have to decline to answer those questions and we expect you to fulfill that responsibility where it i necessary.

TESTIMONY OF DAVID I. SHAPIRO, COURT-APPOINTED EXAMINER IN THE EASTERN AIR LINES BANKRUPTCY CASE

Mr. Shapiro. Thank you, Mr. Chairman. Mr. Chairman, and members of the subcommittee, I do appear here today as the court appointed examiner in the Eastern Air Lines bankruptcy case. It i fair to say that it is highly unusual for a court-appointed official t testify before a congressional committee about an ongoing cour proceeding, and I do so with considerably mixed feelings, and mindful, that as the committee obviously knows, it would be, as th Chairman stated, inappropriate for me to discuss nonpublic detail about the case.

I accepted this committee's invitation to appear because I believ that there are important public interests at stake, and that Congress and the public should be as fully informed as possible abou Eastern's status.

Now I have been in the private practice of law for 40 years during which I have specialized in antitrust, labor relations, an other areas. I am not a bankruptcy lawyer. When Judge Liflan appointed me as examiner, on April 5th of this year, he publicl stated his concern, that all the private parties in the bankruptc case were advancing only their own parochial interests.

The judge recognized, and pointed out the strong public interes in a competitive airline industry, something made more difficult a the number of major domestic carriers dwindles, and in preservin as many jobs as possible.

Judge Lifland's express charter to me was to work with all th parties to achieve a consensual resolution that would put th planes back into the air and the employees back to work.

With this objective, the court directed the parties to move fo ward under my auspices on a number of different tracks, all which occurred simultaneously. Two of these tracks, I believe, are of particular interest to this committee.

Now the first track was to receive and facilitate any potentially viable offers for the purpose of Eastern as a going concern. The second was to assist and to expedite a plan of reorganization under which if there were no sale to a third party, Eastern could still resume more complete operations.

Now proceeding down both these tracks during the beginning of a bankruptcy case is not, as I understand it, how the typical reorganization case works, and this is so because under the bankruptcy code the debtor—in this case, Eastern Air Lines—maintains the exclusive right during the first 120 days to propose its own plan of reorganization.

The typical case does not have an examiner, someone like me, considering other opportunities. This case has clearly been different. I can say, with a great deal of assurance, it has not been "bankruptcy as usual".

Now I have devoted a considerable amount of time to the first of the two tracks I have mentioned, that is, to the effort to facilitate third-party offers. I have done so in the belief that if the parties could agree to the sale of the company to a financially viable purchaser, presenting an operationally viable plan for the airline, its striking employees would return to work, and Eastern could resume flying.

It was fundamental, however, that a serious purchaser would have to submit an operationally viable plan, because the process of restarting an airline, the so-called "ramp-up," is enormously expensive.

And every expert familiar with Eastern's tenuous financial conditions agrees that there is one, only one opportunity to ramp up Eastern. An ill-conceived or ill-managed ramp-up would hopelessly encumber Eastern with additional debts, prejudice the rights of the creditors, and leave liquidation as the only alternative.

Liquidation, of course, would lessen competition in the airline industry even further, and result in the loss of many, many thousands of jobs.

Now, it was likewise fundamental, that any proposal would have to be financially viable. That is, to satisfy Eastern's creditors and to ensure that Eastern would not fail after six months or a year, and return to bankruptcy in even worse shape, again, a virtually certain candidate for liquidation.

Finally, it was also obvious that to achieve a consensual resolution—which is what the judge ordered me to get—a potential buyer of Eastern would have to offer fair consideration to Eastern's equity holder. That is Texas Air.

Now it is beyond the scope of my duties to assess blame in the labor disputes between Eastern's management and its unions.

There is a wide range of opinion about Mr. Lorenzo and Texas Air.

But Texas Air owns Eastern, and elemental due process requires that Texas Air receive fair compensation for its stock. Moreover, it was my hope that someone would offer Texas Air a deal that it could not refuse, consistent with its fiduciary obligations to Eastern's creditors, and Eastern's preferred stockholders.

Now as I have stated, I have spent a great deal of time over the past three months trying to identify and assist potential buyers. My highly experienced expert, Mr. Harry Kimbriel, who was recommended to me both by Eastern and by the pilots union expert as being the best operations man in the field, assisted me in this process.

I told each potential purchaser what I believed would be necessary to achieve the consent of the parties. An operationally viable plan, a financially viable plan, and fair consideration to Texas Air.

During this period, Eastern has been the most advertised piece of property in the United States, yet no one, no one has stepped forward with the basic minimal components of a bona-fide offer to buy and operate Eastern as a competitive carrier.

I have heard from a poet and an inventor; from a hotel magnate and a real-estate investor; and from scores of other persons, most of them well-intentioned, and many of them public-spirited, but none of them willing and able to put a deal together.

Unfortunately, the sad truth is that Eastern has such a significant debt problem that it is not an inviting piece of property for investment.

The two groups that appeared most promising, after the Ueberroth deal collapsed, were headed by Mr. Joseph Ritchie, aided by Shearson Lehman Hutton, and by Mr. William Howard in conjunction with Prudential-Bache.

The Howard group proposed at the outset what amounted to a leveraged buyout. Mr. Ritchie offered $25 million. These proposals would have saddled the company with even more debt than currently exists.

One of my law partners remarked that if such deals were satisfactory, his 5-year-old daughter could buy the airline. But they were not satisfactory. Both the Ritchie group and the Howard group subsequently worked hard to raise equity to inject into the airline.

And again, I believe they were well-motivated, but the principal source of funds these groups were able to tap in their attempts to reach a minimal $100 million level (approximately a third of the estimated cost of the ramp-up, without which this airline does not get into the air at all, was through Eastern's unions), and this created different problems.

For understandable political reasons—and I fully sympathize with them, as I am sure, during the questioning you will see my point of view on this—the unions were adamant that any resuscitated Eastern in which they would invest would have to be almost as large as the Eastern that went into bankruptcy. That is, with something approaching 28,000 employees, and if you cut off 4,000 for purposes of attrition, you are talking about perhaps 24,000 employees.

As a consequence, despite repeated advice from experts, that structural changes in Eastern were essential to revive the company, the operational plans presented by the Ritchie and Howard groups contemplated no fundamental structural changes.

Such changes are necessary for the simple reason that Eastern cannot continue as a viable airline under the debt load that currently exists. Major assets have to be sold to reduce the enormous interest burden on the company and the company needs to retrench to at least a comparatively, competitively safe environment, like Atlanta, where it does not compete head-to-head with such giants as American and United, until it is sufficiently healthy to regrow.

Now I suggested to the Ritchie and Howard groups, that if they combined forces they might be able to overcome their financial problems and share other resources.

For example, late in the process, the Ritchie group lacked the involvement of an experienced airline operator like Mr. Howard, and I spent some time, and great effort, trying to facilitate these groups coming together.

But for reasons that are extraneous to this hearing, they refused to come together. Moreover, despite repeated advice to do so, neither of them went to Eastern's owner to propose a deal that either the owner would find inviting, or that the court could deem to be so reasonable, that Texas Air's refusal of it would be evidence of bad faith, and give me an opportunity to do something about it.

I did not have the tools to work with because they did not follow my advice to go to Mr. Lorenzo, and quite frankly, in the vernacular, make him an offer he could not refuse.

Upon my recommendations, and over Eastern's heated objections, the court extended deadline after deadline to allow these groups to come up with something solid.

I made these recommendations with the awareness that in the process the court might be encouraging the striking unions to hold out against Eastern. The court, nevertheless, resolved to explore every opportunity to allow third parties to purchase Eastern and to get it flying again.

At one time or another in this process I have received loud complaints from every constituency. From the creditors and Eastern, that I was interfering with their prerogatives. From the unions and potential suitors, that I was not quite sensitive enough to their concerns and well-meaning intentions.

I would like to think that the fact that I received complaints from each of the special interests in this case reflects that I have kept my eye on the greater public interest as I was charged by the court to do.

Finally, considerable time has been spent analyzing the business plan which Eastern has proposed. As you are undoubtedly aware, that plan envisions a down-sized Eastern, one with only about 17,000 employees, at least at the outset.

I have publicly stated that my expert and I have concluded, as a preliminary matter, that that plan is financially and operationally viable, with certain caveats, such as Eastern's ability to recruit the pilots it needs, and guarantees that Eastern will not upstream any more money or assets to Texas Air.

These past months have left me with a reluctant but firm conviction that only two practical alternatives remain in this case.

The first is a reorganization plan premised on a smaller Eastern Ai Lines. The second is liquidation.

Gentlemen, I intend to use all of my energies to oppose a liquidation by Mr. Lorenzo, the creditors, the unions, or anyone else, or a

best copy available

combination of all of them. The public interest demands that I do so.

To be sure, a down-sized Eastern means the loss of a large number of jobs that existed in the pre-bankruptcy Eastern, but it is the opinion of Mr. Kimbriel and other experts that some downsizing is necessary, and it is my hope that Eastern's unions will come to accept this as a reality.

Now I sincerely regret I cannot paint a more optimistic picture for this committee, but a bankrupt airline in the highly competitive post-regulation domestic airline industry is forced to make tough choices, whoever runs it, just as Congress is forced to make tough choices in the face of an enormous deficit.

You know the problem: some programs are cut so that others can flourish, and the same harsh truth holds here. Unfortunately, some jobs will be lost so that the majority can be saved, and so that the opportunity for a strengthened Eastern to expand competitively in the future, with even a greater work force, can be preserved.

I hold out only one ray of hope in this somewhat bleak picture I have painted. This past week, I have been meeting with both the company and the pilots union in an attempt to resolve their underlying labor dispute, and these talks will continue over the July 4th weekend. And next week, the talks will expand to include tandem but separate negotiations with the Machinists and the flight attendants.

With a little luck, with a willingness to compromise on all sides, and with a lot of prayer, we may yet settle these strikes and get this airline back into the air.

Now I thank the Chairman and the members of the subcommittee for this opportunity to provide an overview of these aspects of the case and I welcome any questions you may have.

Mr. **Oberstar**. Thank you, Mr. Shapiro. You have certainly given us a very clear-cut statement, a very objective assessment of where the bankruptcy proceeding stands, and the positions of the various parties. It has been most helpful and delivered in a very clear, forthright, and authoritative manner.

The bankruptcy code requires the court to consider the public interest. You have addressed yourself to that I think very well, very clearly.

Mr. **Shapiro**. Let me say this, Mr. Chairman: That is the view of Judge Lifland. It is also my view. But I would say that there are bankruptcy lawyers who have taken issue both with the examiner and Judge Lifland on this issue, particularly the lawyers for the creditors and the lawyers for Eastern, and if you wanted to make the issue clearer, in the sense of putting the stamp, "public interest," in those words, in the bankruptcy code, I am sure you would make it plain for everybody to see that public interest is part of every statute of the United States, including the bankruptcy ones.

Mr. **Oberstar**. Well, thank you. You anticipated where I was heading, because I was going to say that public interest is made very clear in railroad reorganizations, and is not quite as clear about airline reorganization, and I wanted to ask whether the court felt that it had adequate legal authority to consider public interest, even though it has moved ahead and done so.

I think your counsel is very good and very wise, and we will pass that comment on to the Judiciary Committee, and keep it in mind ourselves when we have further bankruptcy legislation reaching the House Floor.

In your evaluation of this case, you have several times referred to fair consideration for Texas Air. You have set up a three-part test of what will constitute a viable plan of reorganization and one-third of that test is, who decides what is a fair consideration for Texas Air, and how do you get to that point? I am just talking process-wise.

Mr. **Shapiro**. Well, in the context of this particular case, I have to give you a little bit of history, to put, in effect, some meat on those particular bones.

Shortly after the Ueberroth deal collapsed, there was a meeting at the office of the counsel of the creditors committee at which were counsel for the creditors committee, its particular experts; counsel for all the unions; and counsel for the debtor.

And under the judge's instructions I laid out a sequence of steps that we would undertake in order to secure a viable proposal for Eastern Air Lines from some third party.

And I made clear that the process was to proceed as follows. That once a viable bidder was identified and he could put together a viable operational plan or business plan, he would then have to approach the debtor—Mr. Lorenzo, in this case—and make him an offer.

That offer, I hoped would be—and I said it very plainly—would have to be good enough to get him to the bargaining table. Because what we are talking about is a consensual arrangement. Once we got him to the bargaining table, we would be engaged in a four-way negotiation. There would be Mr. Lorenzo or his counsel; counsel for the creditors committee; counsel for the unions; and myself. And, of course, counsel for the purchaser.

And in that process, we would attempt to hammer out an agreement that all of those interests could agree upon. But I said the first order of business is to go to the debtor, and get him to engage in the negotiation process.

Now you have heard it said that I had determined that there was a conflict of interest in this case, and there is, in a technical-legal sense, in my judgment, a conflict of interest in this case.

But notwithstanding that, in order for me to have the tools to do anything about, in effect, asking the court to move with regard to the question of another purchaser, there had to be several things. There had to be a viable purchaser out there, and there had to be bad faith by Mr. Lorenzo.

There could not be any evidence of bad faith by Mr. Lorenzo until a purchaser went to him with an offer so good, that his refusal of it could be considered aberrational, and if it was aberrational, then I could do something about it. But if it was not, there was nothing I could do, given the instructions I had, in the first instance, to get a consensual arrangement. That is how that process was to work.

Mr. **Oberstar**. What could you do if Mr. Lorenzo were determined to be in bad faith?

Mr. **Shapiro**. I could ask for the appointment of a trustee because he then would not be acting in the best interests of the debtor's estate.

Mr. **Oberstar**. Thank you.

Mr. **Shapiro**. And without that finding of bad faith, I could not do a thing.

Mr. **Oberstar**. We will have to suspend, at this point, to respond to the second call of a recorded vote on the House Floor, and resume in, roughly, 15 minutes.

[Recess.]

Mr. **Oberstar**. When we broke, Mr. Shapiro, we were discussing the issue of bad faith. That is, the debtor-in-possession at some point reaches a decision on whether offers are, from his standpoint, sufficient, adequate, for him to accept, and you were discussing an offer that would be so good, that Mr. Lorenzo's refusal—in this particular case—would be considered bad faith. Would you discuss, again, who makes that judgment when we get to that point.

Mr. **Shapiro**. Well, let me put it in the context of this particular issue, and how this came about. In the Ueberroth proposal, which, given a number of things—forgiveness of notes and other assets, plus $200 million in cash—there was $464 million.

The problem with the Ueberroth proposal, as Mr. Ritchie correctly pointed out, was that there was no—what we are calling in the trade a "back-end lockup". In other words, it was simply an option to see whether or not the ramp-up would succeed, and if Mr. Ueberroth liked the success of the ramp-up, then he would close on the deal, $464 million in cash and assets would pass, and then he would own an airline.

If he did not like the progress of the ramp-up, he could walk away and Mr. Lorenzo would be left with the airline, and of course, under the Ueberroth proposal, if the employees had come back to work for Mr. Ueberroth in the meantime, and Mr. Ueberroth walked away, the employees would again be facing Mr. Lorenzo and their strike would have been broken.

That was the whole reason why the Ueberroth deal failed, because I could not persuade Mr. Ueberroth to give up his option to walk away.

Now, I said to Mr. Ritchie, we have here an asset which is wasting away to the tune of $1.7 million a day. If you go in with the Ueberroth proposal and add the back-end lockup to it, so that you will own this airline, that deal was so good, that Mr. Lorenzo accepted it in the first instance. If he turned it down now, given the fact that he had previously accepted it, I would have at least prima-facie evidence to argue that he was not acting in the best interests of the estate.

But the question of how much shows good faith or bad faith in a different context is something which, in terms of a consensual deal, does not ever come into play. In a situation in bankruptcy, as I understand it, once a plan of reorganization is proposed, there is nothing to stop someone else from coming in with his own plan of reorganization.

And Mr. Ritchie, after the plans of reorganization have been filed, and the debtor's exclusivity has expired, can very well come in and offer an opposing plan of reorganization. And there will undoubtedly be a proceeding and litigation with regard to which is the better plan. But of course that will involve litigation on the issue of valuation, and depending on who is counting in this particular case, the value of Eastern's assets is anything from $4 billion to $6 billion.

So the question is how much are these assets worth, and how much, in view of the assets that are there, am I entitled to ask for my stock in the airline. That is a big, long, expensive litigation. Now what happens?

With an asset that is wasting away to the tune of $1.7 million a day, litigation might be successful, but at the end of the process you might be left with a beat-up engine and some spare parts. This airline would have died. That is why this judge has been insisting on a consensual deal, and that is the basic technical problem that we have when we are dealing with a wasting asset, and with employees out on the street for, lo, these four months now.

Mr. **Oberstar**. That is a very helpful insight into the process, and how it is working, and why things are happening and the way they are working.

While I have a number of other questions, I want to get to one issue that troubles those of us who are not bankruptcy experts, and I think those who are inside the process—the pilots, the mechanics, the flight attendants, and the traveling public.

The disposition of assets, the selling off of assets. Are there judicial constraints on Mr. Lorenzo's ability to dispose of those assets?

Mr. **Shapiro**. Yes.

Mr. **Oberstar**. And whose interest is represented in the disposition of those assets? The creditors? The debtor? The public interest?

Mr. **Shapiro**. All of the above, including, also, the employees who have been resisting the sale of each and every asset that has been offered for sale.

Mr. **Oberstar**. Can Mr. Lorenzo simply sell the assets without having to clear it first with the court, with the examiner?

Mr. **Shapiro**. No. He cannot sell any assets without a court order, which he has to get on the basis of a factual hearing, to have the court come to a decision that the asset sales are in the best interests of the estate.

Mr. **Oberstar**. Let me yield myself another minute or two to let you expand upon that answer, and if you could just take us through, step by step, the process involved.

In short, Mr. Lorenzo, you have said, now, cannot just simply talk to his airline, Continental, and say we have some Eastern aircraft for sale or some Eastern engines for sale, what is your price?, and buy them off Eastern. He has to go through the court. Tell us how that happens.

Mr. **Shapiro**. First of all, there has to be a deal made to sell the assets. Then there is a motion made to the court. Let's take the Trump Shuttle, for example, which, at one time, was known as the Eastern Shuttle.

There was an offer by Mr. Trump to buy the shuttle. I do not remember the exact terms—whether it was $350 million some-odd dollars, or something more than that. $365 million.

And then there was a proposal by Eastern, that in view of the fact that it was losing cash so rapidly, and that its cash position was expiring, it needed the cash from the asset sale to be able to maintain itself while it tried to get back into the air.

Now the creditors came in and took a position and said, well, this asset sale will be very helpful in paying off the some $3 billion in debt you owe us, so we will consent that you sell it, but you put that money in escrow and we will only dole out so much of the cash that is in escrow as will enable you to keep going.

The unions came in and said, we do not want you to sell any of these assets, at all, and the judge held a hearing on the facts as to whether or not it was in the best interests of the estate to sell the shuttle, and then there was, in effect, an attempt to get the highest and best bid for these particular assets.

And sure enough, America West came in and attempted to get the shuttle aircraft, and the shuttle rights, and tried to outbid Mr. Trump for it. But unfortunately for the estate—but luckily for the unions involved—America West, you know, is nonunion, and Mr. Trump was operating a union airline.

The fact is that America West could not get the financing, and so, in the auction process, its bid failed and Mr. Trump got the shuttle, and that is the reason you now have a Trump Shuttle instead of the old Eastern Shuttle.

Mr. OBERSTAR. Is consideration given to whether the sale of any particular asset, whether it is a particular aircraft, or aircraft parts, would reduce Eastern below this term we have heard so often—below the point of "critical mass" to operate an airline competitively?

Mr. SHAPIRO. I do not think there is any question but that that would be a consideration, but in any of the proceedings to which I have been witness, there has been no attempt to make out such a case, and none of those arguments have been advanced in connection with the sale of the assets so far. Whether they will be made in connection with any future sales, I do not know.

The argument has been made that you should not consider a sale of these assets outside the plan of reorganization.

Now that is the argument that has been made. The counter-argument that has been made by the company and the creditors is that this is in the best interests of the estate because the offers for these assets were so good and the estate was in such bad shape that they needed the cash. The company and the creditors won those arguments.

Mr. OBERSTAR. Thank you. I have exceeded my time, but I wanted to get those points on the record. Mr. Clinger.

Mr. CLINGER. Thank you very much, Mr. Chairman, and thank you, Mr. Shapiro, for a very excellent explanation running us through the process and how the procedure is working.

I want to explore, just a little bit, this potential conflict between—on the one hand, the rights and the duty to the creditors and to the stockholders, and on the other hand, the public interest, and you have indicated that in all things the public interest is weighed in the process.

Is there a priority here, though? Because it seems to me that there could come a situation where you would have to weigh the public interest against the rights of the creditors.

I am thinking of a situation where you might have to face a decision where liquidation would produce some cash in hand, where the creditors are going to be taken care of. A potential buyer to operate the airline poses some risk. Maybe it is an acceptable risk, but nevertheless, a risk. How do you come down, in that kind of a potential conflict?

Mr. **Shapiro**. I will tell you this, Mr. Clinger: That from what I have seen of this judge, there is no question but that the public interest is right smack in the forefront of his vision in terms of the issues involved in this proceeding, and I can tell you also that they are right smack in front of my vision.

Now that does not happen to be the unanimous view of the bankruptcy bar. I have been told that there are no such words as "public interest" in the bankruptcy code when we are dealing with in Chapter 11, and I have taken a position that "public interest" is written into every statute that this Congress has ever passed.

Mr. **Clinger**. Well, that is very heartening, very encouraging to hear, because obviously, that is our interest as a committee here. I think our only interest in this hearing is to determine if in fact the public interest is being served by processes now ongoing.

Let me ask you this: Mr. Ritchie has indicated that in fact, over the long pull, there will be about $300 million capital put into this operation—not $100 million.

[Laughter.]

Why is that not sufficient? Why did you feel that that was not viable?

Mr. **Shapiro**. Let me explain why. As I understand it—and I am of course subject to correction by Mr. Harris of Shearson Lehman—what I heard him say was that there was a $100 million of equity to be put in, and the balance of some $200 million of capital, which was to be raised by increasing the debt load.

You might be interested to know that I have asked Mr. Harris, in connection with the Ritchie proposal, whether he would provide me with a highly confident letter, that they would be able to raise—not $200 million but $175 million. Somehow I would make the deal work if I had the $175 million, and all I needed was a highly confident letter. I do not have it to this day, Mr. Clinger.

Mr. **Clinger**. Do you take into account the human factor here? The Ritchie folks make the proposition that no matter what happens under the Lorenzo regime, this is not a viable operation because the well is so poisoned, the atmosphere is so bad, the human factors are so overwhelming, that no matter what happens this thing cannot survive, and that on the other hand, with new management, more sympathetic, more understanding, sensitive to their concerns, that this should be taken into account.

Mr. **Shapiro**. It is very difficult to weigh the question of labor-management relations, and bitterness between labor, on the one hand, and management, on the other, in terms of whether or not you are going to get a successful operation.

It is very hard to put an objective fix on that. But I do believe Mr. Ritchie has this point, and it is a solid one. It is clear that the atmosphere between the unions, on the one hand, and the employer, on the other, is poisoned, and it is likewise clear that it is my job, as the examiner, that despite that poisoned well, to try to get these parties together in a cooperative effort.

Now this may be a fool's goal. It may never be able to be achieved, but I sure as heck am going to try.

Mr. CLINGER. Just one final question. As a final shot, Mr. Ritchie has indicated that if you, and the judge, feel that their plan is too ambitious and is not going to work because of the increased debt load that would be required, that they would go with the Lorenzo plan, they would duplicate the Lorenzo plan, asset sales and so forth, and then the one difference would be that you would have a happier labor force under that plan than you would under——

Mr. SHAPIRO. I could not agree more. However, you still have to buy the stock of Eastern Air Lines from Mr. Lorenzo, and Mr. Ritchie has not given him an offer that he could not refuse, as a result of which I have had nothing to work with.

Mr. CLINGER. I understand. Thank you very much.

Mr. OBERSTAR. The Chair is going to reverse the order of questioning by members, and begin with the last, and will recognize the gentleman from Georgia. Mr. Jones.

Mr. JONES. The last shall be first. Thank you. I just had one question, and want to clear up, if you could, some confusion that I had, Mr. Shapiro, in regards to what we will call the Ueberroth deal.

It seems to me that I heard Lorenzo implying that that deal did not work because the unions insisted on a trustee, and I seem to be hearing from others that no, it was not the union, but it was perhaps your idea, and I just wondered if you would——

Mr. SHAPIRO. It was my idea, Mr. Jones.

Mr. JONES. It was not the unions who insisted?

Mr. SHAPIRO. Well, let me put it to you this way. In the heated discussions that ensued over at the IAM headquarters, and later, in my office, over those three-four days, around the clock, it became very clear to me that the Machinists, under no circumstances, would go back to work for Mr. Lorenzo.

And I could not get them to budge in terms of the concessions that they were talking about in order to make the Ueberroth deal work. On the other hand, it was likewise clear to me that I had to have some kind of method to persuade Mr. Ueberroth to give up his option, and in effect become the real "live buyer" of this airline.

That he was going to pay—and he had no money at risk in this of his own. This was borrowed money. If he would pay the price, and he would own the airline, and Mr. Lorenzo would walk away, but walk away and not be able to come back.

And I said the only way I can accomplish this, in order to persuade Mr. Ueberroth to give up that option, and agree to a back-end lockup, and to get these concessions at one and the same time, was to come up with the idea of a trustee. And we did come up with the idea of a trustee, and we did get the concessions. And then we called the company in, and interestingly enough, although Eastern's counsel was screaming bloody murder about the notion of the trustee, Mr. Lorenzo was prepared to negotiate with regard to the question of interim control, and he did negotiate with Mr. Ueberroth on the subject of interim control while it was proceeding through bankruptcy.

But Mr. Ueberroth refused to negotiate on the question of giving up his option, and an interesting thing happened. We were meeting at the Vista Hotel, and Mr. Miller, who was counsel for Eastern Air Lines, and I, went to see Mr. Ueberroth, and we said, "listen, if you will give up the option and agree to a back-end lockup, maybe we can knock $90 million to $100 million off this price."

And Mr. Ueberroth's response to me was: "I don't talk to emissaries." And the deal failed, and it failed because of him. That is the truth, Mr. Jones, no matter what you have heard to the contrary.

Mr. **Jones**. I thank you for that very revealing insight. Thank you, Mr. Chairman.

Mr. **Oberstar**. Mr. Molinari.

Mr. **Molinari**. I would like to join in in expressing our gratitude to you for simplifying some very, very complex issues for us. There is one area that I would like to try to clear up in my own mind, and that is this. Obviously there is a great deal of attraction to the concept of employee ownership, particularly in view of what has transpired, historically, between management and labor in this case.

The $100 million offer, from your standpoint, is below that basic minimal figure you mentioned in your testimony. Therefore, you do not think it is operationally feasible. But you did indicate in your testimony, that if they were to come to about $175 million, plus—if I understood you correctly—agree to some fundamentally structural changes—and I take that to mean that depending upon the success or failure of the operation, that they would agree to cut down on the number of employees or personnel. That that might have a chance of succeeding. Am I understanding you correctly?

Mr. **Shapiro**. Yes and no. Let me put it this way. There are two distinct things to be considered here. One is operational viability. That is, for example, where you fly, what are your load factors going to look like, what is your competition going to be in terms of the routes you pick, how fast you ramp up the airline, what kind of marketing you are going to be able to do to get the passengers into the aircraft after you have been, in effect, out of the market for so long.

That is ramp-up and operational viability. Ramp-up is the short term, and in the long term, we are talking about operational viability.

Mr. **Molinari**. And what would that ramp-up cost amount to, roughly?

Mr. **Shapiro**. It is our estimate that you have got to be looking at $300 million to ramp-up this airline. Everybody agrees it is a very expensive, risky proposition. That is the ramp-up, operational viability.

The second problem is financial viability. Now, depending upon who is counting, as I say, when you have got asset valuations of $4 billion to $6 billion, and over $3 billion in debt, you have got to be in a position, financially, to get rid of some of this debt load. You cannot carry it on the back of this operation. It is a very difficult thing to do.

The interest costs alone would turn what would otherwise be a very profitable operation into a sure candidate for extinction. So, Eastern, as a practical proposition, has got to get rid of some of that debt load. They are proposing, in their case, to do it by selling $1.8 billion worth of assets.

Now, you can argue—listen, do not sell that $1.8 billion of assets. Let's put more equity into the company. If we put $100 million of equity—that means risk capital, not junk-bond money, which is more debt—but actual equity investment into the company. Risk capital, at the bottom of the line. The fellow is taking a risk. If it goes wrong, he loses the whole stake.

You put in $100 million, and then what you do is you talk about raising—raising another $200 million from employee concessions, which is what the unions are proposing in this case—and I think they have to be lauded for their attempt to save this airline. I mean, these people really care.

Then you are in a position to say, well, maybe we do not have to pay down all of that debt right away, and maybe we can get this airline back into the air on a financially viable basis.

So you have two problems to answer: The financial viability and the operational viability. According to my experts and me, Mr. Ritchie's plan flunked on operational viability and he also flunked, and is still flunking, on financial viability.

If he had a plan that would pass my experts, I could go to the court with it. I would be doing that today, and we would not be having this hearing.

Mr. MOLINARI. I see the red light is on. I would just like to ask one quick, short question. Then, what you are telling us is that for any plan to be submitted, that would meet your recommended approval, there would have to be a recommendation or a proposal to sell $1.8 billion in assets?

Mr. SHAPIRO. Well, whether it be $1.8, or what other number——

Mr. MOLINARI. Some substantial sum.

Mr. SHAPIRO. But there would have to be a significant number, because, in essence, what you are trying to do is get a consensual plan. You are trying to get the creditors and the preferred stockholders, and the debtor—everybody—to agree that this is a plan that we can go with in reorganization. The price for getting the creditors to go along has been, in practical terms, a commitment to sell $1.8 billion worth of assets, which pays them—I do not know what the percentage is—but close to a third, or maybe more than a third of their outstanding debt.

Mr. MOLINARI. Thank you. Thank you, Mr. Chairman.

Mr. OBERSTAR. Thank you. The Chair recognizes the gentleman from California. Mr. Mineta.

Mr. MINETA. Thank you very much, Mr. Chairman. Mr. Shapiro, thank you very much for your appearance here today. Have you had an opportunity, now, to evaluate any of the concessions that were in the proposal for—under the Ritchie proposal?

Mr. SHAPIRO. We looked at them. Yes.

Mr. **Mineta**. And were you able to, in your charge, go back to any of the transfer of the assets, prior to the filing of the Chapter 11?

Mr. **Shapiro**. Do you mean whether or not we are conducting an investigation into what is now known as the pre-petition transfers?

Mr. **Mineta**. Yes.

Mr. **Shapiro**. That is one of the three tracks that we are on, and a subject which I cannot discuss because that investigation is ongoing. We are investigating, very vigorously, the subject of the prepetition transactions, and I am simply not in a position to comment about that.

Mr. **Mineta**. And what about the issue of the debtor-in-possession being allowed to continue the management of the company? Is that just in the judge's hands, to make that determination?

Mr. **Shapiro**. It is in the judge's hands, and this judge has the public interest right up here.

Mr. **Mineta**. But in this instance, he decided not to appoint a receiver and allowed the existing management to stay in place while going through the Chapter 11 proceedings?

Mr. **Shapiro**. Well, let me put it to you this way. It came up two times. The first time it came up was in connection with the Ueberroth proposal, and it is true that I did ask the judge to appoint a trustee for the purpose of—as I told Mr. Jones—getting agreement both on the question of interim control and on the question of getting Mr. Ueberroth to give up his option to walk away.

And the judge said no, he would not appoint a trustee, which he believed was a very drastic remedy. He would much prefer that the parties work out a consensual resolution. It turns out that the judge was right in that instance, because what happened was—you see, Mr. Ueberroth was not a party to the proceeding, and we could add all the trustees in the world, but he was not going to agree to give up his option, and that is the reason that he did not buy the airline, and that that deal failed.

Mr. **Mineta**. But in trying to reach that consensual resolution, is not there sort of a burden that the people who are trying to find an alternative approach have to overcome, in the sense that the judge is saying, well, put the airplanes back into the air, put the people back to work? Again, if it is a——

Mr. **Shapiro**. He has to find that the debtor is acting in such a way as to be injuring the estate.

Mr. **Mineta**. But if, at the same time, they have got a $914 million debt, and they are going to sell $1.8 billion of assets to satisfy those debts, what is going to be left of the corpus for anyone to work with?

Mr. **Shapiro**. Well, let me tell you what I understand will be left, but let's get the numbers straight. The numbers are that there is approximately $3 billion of debt. There is a proposal to sell $1.8 billion worth of assets. The company may be worth somewhere between $4 billion and $6 billion, depending on who is counting. Now we have that.

What will be left, as I understand the plan of reorganization, which I believe will be filed some time within the next several weeks—and I do not know this, but I have a hunch it will be filed as a consensual plan with the creditors' approval. I said I do not know this but I have a hunch.

What will happen is that you will have an airline which will not be 28,000 people. It will be 17,000 people. It will have its main hub in Atlanta, where it will be competing head-to-head with Delta, and the hub which it previously had in Miami, which will remain as a station, will not be the center of Eastern's activity. That is what you will have left.

The question remains whether or not that "bird will fly". It is the judgment of my expert, who was appointed—let me repeat, Mr. Mineta, not merely with the concurrence of Eastern, but on the recommendation of the expert hired by the pilots union, a man who is highly respected in this industry. That expert, Mr. Kimbriel, was said by Mr. Kupersmith to be perhaps the foremost operations man in the business. It is Mr. Kimbriel's view that if he had $1 billion to put into this airline, he would not start it up any differently than the way Eastern is starting it up now.

Mr. **Mineta**. I am sorry. He would——

Mr. **Shapiro**. If he had $1 billion to put into this airline, he would ramp up this airline in exactly the way that Eastern is doing it now.

Now let me say this. There is a substantial question about the South American routes. There are 800 to 900 jobs in those South American routes. If I could have saved those 800 to 900 jobs, I would have walked across the country barefoot to do it. The question is simply this: I could not get—I could not get the experts to tell me that the call on giving up the South American routes was a bad call. I could not get an independent expert to tell me—although it is questionable—that the company's judgment in this respect was so clearly wrong, that I could go to the court and say stop. By the way, those routes have not yet been sold.

Eastern is still considering it. That issue is still open. It has not yet been resolved. But I will tell you, right now, we spent at least 10 days on this very one issue, trying to come up with an alternative solution and we have not yet been able to do so.

Mr. **Mineta**. Well, it seems to me, based on the general proposition that Eastern has proposed—namely, the sale of assets to repay debt, operating a down-sized operation of 157 aircraft serving 77 cities, the sale of the South American-Caribbean and Canadian routes, abandoning, so to speak, the Miami hub, concentrating that at Atlanta, and then superimposing upon that your four assumptions that in terms of a test, that there would be no recession in the U.S. economy, that Eastern would meet its target of employing 1700 pilots, that there would be a large amount of cash available to Eastern that would be tightly controlled for start-up and operations.

And fourthly, that Texas Air would not seek to use any Eastern Air assets to solve its own problems. I am just wondering whether or not there is going to be any opportunity for an outsider to come in to buy and take over the operation.

I am wondering if we are not caught in a Catch-22 proposition.

Mr. **Oberstar**. The Chair would like to observe that we have roughly five minutes remaining. Defer this response until we return from this recorded vote. The Committee will stand at brief recess.

[Recess.]

Mr. **Oberstar**. Mr. Shapiro, when we broke the question had been posed and you were about to answer. The question is in the record, we need not repeat it. Please state your response and then we will pass to Mr. Stangeland.

Mr. **Shapiro**. I have thought about Mr. Mineta's question during the recess.

Mr. **Oberstar**. Please, people in the rear of the room, close the doors to the hallway.

Mr. **Shapiro**. I have been thinking about Mr. Mineta's question during the recess and the best answer to it is this. Unfortunately, we are caught between the dilemma of a consensual arrangement on the one hand which requires the consent of all the competing parties under which there might not be room for a third party to come in and buy the airline.

On the other hand, if we were talking about a litigated solution, there might very well be an opportunity for a third party to buy the airline. That is, there would be a competing plan filed after the plan filed by the debtor. There would be an attempt to convince the court that the alternative plan or the competing plan was a better plan. There would undoubtedly be a long-term litigation dealing with issues primarily of evaluation involving all kinds of experts and all kinds of disputes and that litigation would not be resolved in time enough to save Eastern. That is the problem.

Mr. **Mineta**. But Mr. Shapiro in examining the Ueberroth proposal you found it lacking. In looking at the Ritchie proposal you found it lacking. Who is going to take a look at what Lorenzo did to this airline that got it to its present point? [Applause.]

Mr. **Shapiro**. Two people in the first instance. I am already looking at what Mr. Lorenzo did to this airline. There is an ongoing investigation with regard with what is known as the pre-petition transactions. There are at least eight people in my office who as we speak are pouring over thousands of documents and further than that I cannot tell you what is going to happen with regard to that investigation because, one, it has not been completed and, two, it would be improper for me to do so.

Mr. **Mineta**. Thank you very much, Mr. Shapiro. Thank you, Mr. Chairman.

Mr. **Oberstar**. The Chair recognizes the gentleman from Minnesota, Mr. Stangeland.

Mr. **Stangeland**. Thank you, Mr. Chairman. I do not have a question, but I do have a comment. And I want to thank you, Mr. Shapiro, for appearing here and being so very candid. I think you shed a lot of light on the problems that face this whole question of whether or not Eastern flies again. I just have to believe that you are between a very very large boat in an extremely hard place. You have the public interest here and you should have. And the competing concerns, an employee's union that will not fly for Lorenzo. They do not want to downsize for obvious reasons, and you cannot find somebody to pump in the risk capital that is needed to make that a viable airline.

It sounds to me like if Eastern ever flies again, you will be elevated to sainthood. Your job sounds to me about equal or on a par with Moses when he had to part the Red Sea, and I wish you well. I commend you for already having the pilots now in the conversation. I wish you well in getting the other employees in the conversation. I also have some faith here that if anybody can do it, you probably are the one to do it. But it is a monumental task.

Mr. **Shapiro**. Thank you very much, sir. I would not exactly go as far as you did, but we are going to try.

Mr. **Oberstar**. The gentleman from California, Mr. Bosco.

Mr. **Bosco**. Thank you, Mr. Chairman. And I also thank you Mr. Shapiro for your testimony. But in all due respect, I really have not heard before me a more one-sided procedure than this appears to be. And I am not questioning your judgment, I am just taking a look at what the law apparently steers everyone toward in bankruptcy.

I mean, here we have a case where the debtor did not want a trustee and the court did not appoint a trustee. The debtor wanted to sell off assets on several different occasions. The court sold off the assets. The debtor wants to downsize the airline, but your conclusion is the airline should be downsized. The debtor, many people believe wants to liquidate the airline, that is your other possibility as posited here.

The only other remedy there could possibly be for a third party is to come in after the period of exclusivity has ended and make a bid for this airline. And in that case, you say it could go into years of litigation in which the airline will be gone by the time the litigation is over with.

The last possibility is a consensual agreement that only one person has to agree with and that is the debtor. I mean, let me declare bankruptcy some day. This sounds like the best possible way for anyone to accomplish the ruination of an airline. Now under what circumstances, if for instance Mr. Ritchie came to you with exactly the same—or anyone else for that matter—with exactly the same plan as Mr. Lorenzo, you could not accept it, could you?

Mr. **Shapiro**. That is not correct.

Mr. **Bosco**. Under what circumstances could you accept it?

Mr. **Shapiro**. Any one of a number. And let me put it to you this way. Let me tell you what I told Mr. Ritchie, and maybe that will answer your question. I thought I had already testified to that, but perhaps, it bears repeating. I said, one, you come in with an operationally viable plan, and by the way if you are smart, what you will do, is come in with a carbon copy of the Lorenzo proposal so nobody can criticize that it is not—at least the debtor cannot pooh-pooh it on the grounds that it is not operationally viable. If you are smart tactically, that is what you will do.

The second thing you have to do is show that you have, in terms of invested capital in this airline, $100 million at risk. Once that is done, there may be ways to raise the additional $200 million in cash, either through employee concessions or what have you, to be able to buyout Mr. Lorenzo's interest. And if you will agree to a back end lock-up, in other words, you will buy the airline in fact and you will offer Mr. Lorenzo precisely what the Ueberroth deal was, since he accepted the Ueberroth deal in the first instance, and this is now a wasting asset which on everybody's agreement is not going down to the tune of $1.7 million a day.

If Mr. Lorenzo rejects that proposal and says pooh-pooh, little boy, go away, you will have at least given me the tools to argue to the court that Mr. Lorenzo, at least prima facie, is not acting in the best interest of the estate. If that is so and you give me the tools to work with, I can work. If you do not give me the tools to work with, I cannot get the job done.

Mr. Bosco. Mr. Ritchie testified here earlier that he would be happy to propose the Ueberroth deal, as he said, any day of the week. You are saying that he never did do that.

Mr. **Shapiro**. No, let me make it very clear. What he said was, he would propose the Ueberroth deal as long as he had the option to walk away. I told him he had to propose the Ueberroth deal and get rid of the option to walk away. And if that was the deal that was proposed and it was turned down, I would have something to work with. And without that, I could not make it work.

Mr. Bosco. In terms of the analysis that you and your expert have done, are there working papers or is there some way that we could look at that analysis or maybe the Department of Transportation could or some other party? We have had people here testify that, for instance, that they believe other plans are perfectly feasible. Is there a way that we could get the working papers on what led you to this decision?

Mr. **Shapiro**. Mr. Bosco, let me say, there are working papers and whether or not it would be appropriate for you to ask me for them is an issue I would leave, in the first instance, up to the Chairman, and then I would have to consult with the judge with regard to that.

Mr. Bosco. Apparently a lot has depended on that decision. I mean you have told the judge that other plans are not feasible based apparently on expert advise. There are other experts who say that those plans are feasible. And not that I would ever put myself or this Committee or the Congress into a position of second guessing, but there has got to be a way, perhaps of looking at what analysis went into this decision.

Mr. **Shapiro**. I am sure if the issue comes to the court, there is no question but that the court would look at the analysis. Whether it is appropriate for this Committee or for the Department of Transportation in an ongoing proceeding before a bankruptcy judge to have the court appointed examiner's expert's work papers, is a tough question. I do not have an answer off the top of my head. I could tell you very frankly that I think it raises some substantial issues in terms of separation of powers. And the judge might take the position with regard to this that would not be favorable to my turning the papers over. So I would have to check with him in the first instance and I think there are other basic questions that go to this issue.

I am here because I am trying to shed as much light on the process as possible, not to engage in a debate as to whether or not one plan is right or another plan is right. I have given you my best judgment and that is all I can do.

Mr. Bosco. Thank you.

Mr. **Oberstar**. The gentleman's time has expired. In that connection, is the Department of Transportation involved in assessing the operational or financial viability of a particular plan? And under the Bankruptcy Code can the Department be involved?

Mr. **Shapiro**. The first question is no. The answer to the first question is no. And the answer to the second question is I do not know.

Mr. **Oberstar**. Thank you. The gentleman from Texas, Mr. Laughlin.

Mr. **Laughlin**. Mr. Shapiro, I know who Frank Lorenzo is. I have never met him and I have never been in his office, but I would say to him if I were to meet him, your picture needs to be on his wall of heros.

Mr. **Shapiro**. I am sorry, I did not hear you, sir.

Mr. **Laughlin**. Your photograph needs to be on his wall of heros if he maintains one in his office, because you are the first witness, other than an employee of his company or the Administration say anything nice about him.

Mr. **Shapiro**. I do not know that I have said anything nice about him at all.

Mr. **Laughlin**. You did not lavish him with praise, but you did say something nice about him. And I am not criticizing you for that, I just wanted you to know that you are in a minority of one since I have been sitting through this hearing.

Mr. **Shapiro**. Let me put it to you this way, Mr. Laughlin, I do not know that I have ever said anything nice about Mr. Lorenzo and I would try to make it very clear that I would not want to say one way or another what my attitude about Mr. Lorenzo is.

Mr. **Laughlin**. I am not asking you to, but based on——

Mr. **Shapiro**. If you did, I would refuse to answer.

Mr. **Laughlin**. I would recognize that and respect it. More seriously, you indicated that if you were to determine if Mr. Lorenzo was not acting in good faith, you would take certain action, and I missed what that action would be, and would like to hear it. And also, what would be your criteria for him not acting in good faith?

Mr. **Shapiro**. I thought I answered this before. I said in the context of an offer, that if an offer had been made to Mr. Lorenzo which he turned down and which would lead me to conclude that his actions could only result in a detriment to the estate. In other words, having previously determined that as a technical legal matter, there was a conflict of interest in terms of his position with regard to his positions with Continental Air, Texas Air, and Eastern, that having previously decided that there was such a conflict, that if he acted toward the estate in a manner that was detrimental to the estate, if he turned down an offer that he had previously accepted in a situation in which we were dealing with a wasting asset, I could conclude—not that I would—but I could conclude, I would be in a position to conclude at least prima facie, that he was acting not in the best interest of the estate. And then I would have the power to go to the judge and say, it is now time, in my judgment, to appoint a trustee.

There would be a hearing on that motion. All of the issues, all of the facts that had been developed up to that point would come before the judge. Mr. Lorenzo and his counsel would undoubtedly make a defense, and a judgment would be rendered by the court as to whether or not at that point he was acting to the detriment of the estate. If the ruling was that he was, he could be removed and a trustee could be put in. If the ruling was that he was not, there would not be a trustee.

The point in all of this is that unfortunately Mr. Ritchie for whatever reasons he had did not give me the tools to get to first base. If I could have gotten to first base, I might have gotten all the way around and home. But I did not even have the tools to get to first base. That is what I am talking about.

Mr. LAUGHLIN. The next item I want to ask you about is in your study of the Eastern reorganization plan. Is it realistic to expect Eastern to downsize and still avoid liquidation?

Mr. SHAPIRO. My expert believes that it can. And I say he has looked at this problem. He has educated me about the process, but he has spent a great deal of time in terms of doing that and I have myself. And let me tell you the thing that drives me among other things. I do not know that any of the experts, the so-called experts hired by the Creditor's Committee who evaluated this airline and there were other experts that evaluated this airline did what I did.

After finding out what Eastern's plan was, I said the only place to go to really get a sense as to whether or not this airline would be operationally viable, is to go to Atlanta. And I went to Atlanta and I visited Eastern's property where they have just about as many gates as Delta, where they have just about as many ticket counters as Delta, and where they have a major repair facility. I did not spend my time talking to the Eastern people, but I talked instead to the travel agents. And what the travel agents told me was that if you start Eastern up in Atlanta, within a matter of months, we, the travel agents, will get Eastern back up to its premarket share.

We are for practical purposes operating here in Atlanta and throughout the Southeast with only one carrier. One person used the term, a monopoly carrier. There are running something like 80 to 90 percent load factors. They are over-booking the airline. They are charging very expensive fares. The judge even remarked that he did not like the kind of price he had to pay for a ticket from Atlanta to New York, and that was—in terms of the absence of competition—this was a matter of great concern to him because there was no price competition throughout the Southeast and along the Eastern corridor.

I came to the conclusion that Eastern had a great opportunity to come in under Delta, compete with Delta, start this airline up in Atlanta, and to grow from there. And I got that sense primarily from talking to the people who sell tickets on airlines. When the experts came in and they themselves re-traced the routes I did, they told me in their expert opinion that what I had sensed—and I have that sense as an anti-trust lawyer—that what I had sensed was in their view actually going to be the case.

I can tell you this much, we have taken a look at Eastern's projections. We believe they have low-balled their projections. We believe they are going to do better than they have told the Creditor's Committee they are going to do. And as a matter of fact, in the first several months that they have put in their business plan, they actually have done better than they told the Creditor's Committee that they were going to do.

Mr. **Oberstar**. The gentleman's time has expired. The Chair recognizes the gentleman from Pennsylvania, Mr. Kolter.

Mr. **Kolter**. Thank you, Mr. Chairman. Mr. Shapiro, we were rather confused here today—I am rather confused. As the Chairman stated, we here, many of us do not understand the workings, the complexities of a bankruptcy court, and you have made a number of decisions evidently. Is there a higher authority in decision-making to settle this problem today that we have with Eastern and New York Air?

Mr. **Shapiro**. Yes.

Mr. **Kolter**. Is there a higher authority than the court? And what is that authority?

Mr. **Shapiro**. Yes. First of all, I have not made a number of decisions. I have not made any decisions. I have made a number of recommendations. The decision-making authority is in the bankruptcy judge. His decisions can be appealed to the District Court from thence to the Court of Appeals and from thence, the Supreme Court of the United States.

Mr. **Kolter**. So there is an appeal process?

Mr. **Shapiro**. No question about it.

Mr. **Kolter**. You evidently have made some decisions or recommendations when you said that the Ritchie plan fails. It flunked. Twice you said it flunked.

Mr. **Shapiro**. That is right. It flunked.

Mr. **Kolter**. How in the world can you make that statement? I mean what is behind that. I do not understand how you can say that his plan has flunked. You know, as I stated with an earlier witness, we have had a number of meetings, this Committee has, in which Eastern Air Lines has testified. And everything they have stated, everything their management people have stated has been hate, has been anti-working people, and they do not give a hang about flying in friendly skies.

Mr. Ritchie in turn, upon his testimony, is totally opposite. He gives us a ray of hope. Yet you say he has flunked. What can we do to help Mr. Ritchie here this afternoon, so he does not flunk? [Applause.]

Mr. **Shapiro**. Let me put it this way. I do not know what you can do. I really do not. I could tell you this much, I do not know anybody who has tried to help Mr. Ritchie succeed more than I have. And I think perhaps if you have a little bit of history about this, you would understand.

I first met Mr. Ritchie in a hotel room at the Drake Hotel sometime about 1:30 in the morning. I think the date was April 24. At that time he expressed an interest in buying Eastern, and I said here is what you have to do. You have to be able to raise at the very least $100 million of equity capital. If you can do that, I will get for you a form of a confidentiality order, and I will get it delivered to you so you can send that confidentiality order to counsel for Eastern Air Lines.

Once you have submitted that confidentiality order and some evidence of the substantiality of your position, I will see to it that you get enough information to enable you to make a meaningful bid.

Mr. Ritchie went away. I made sure, however, he got a copy of that confidentiality order. I did not hear from Mr. Ritchie for weeks.

Mr. Ritchie came back late in the process and again I met with Mr. Ritchie, and I advised Mr. Ritchie as to how to put a plan together. I advised him, both tactically and strategically, about the things I thought he might be able to do in order to accomplish getting the airline. I ran the risk of time after time asking the court for extension after extension after extension of the deadlines, so that Mr. Ritchie could firm up his plan. I worked with his investment advisor. I worked with his other advisors. I had close to 12 to 15 meetings with Mr. Ritchie, at 4 o'clock in the morning and at 8 o'clock in the morning. I was always available to Mr. Ritchie. My expert was always available to Mr. Ritchie. I gave Mr. Ritchie everything I had to give, and I gave him the benefit of my advice.

And what Mr. Ritchie did, for whatever reasons he had, either because he did not have the wherewithal to follow my advice or he had different advice which he preferred to rely on. It turned out that he could not come up with the tools I needed to be able to get to first base in order to be able to have his plan considered by the court.

Mr. **Kolter**. Are you saying there are rules you must follow in order to pass this test?

Mr. **Shapiro**. I am sorry, no. I did not say that at all. I said, you have to have an operationally viable plan. You also have to have a financially viable plan. One of the tests for a financially viable plan is get your investment adviser to give me a highly confident letter that they can raise the money. I said, let them put in whatever caveats he wants to in that letter, but get me a letter saying—and when an investment adviser does that—that has certain implications. That is the ground work for raising the money.

To this day, I have not gotten such a letter. I begged him for it. I said, look at your ramp up. My experts sat down with their people and said, your ramp up is way too fast. It is too risky, slow it down. The way it stands now is where we have got a $300 million at risk in this ramp up, at least meet the basic minimum tests that we are talking about so I can go to the court and say, your plan is operationally viable, your plan is financially viable, get me the highly confident letter, and I will even get you extensions of time to be able to do this.

I have had four different plans delivered to me. Some way past the deadline. I have had one delivered to me in the middle of the night. One delivered to me at 6 o'clock at night. Another delivered to me at 12 noon. And then to be told in the court house, "oh, that is not the plan, we have a different plan." And repeatedly, even though I knew that I was running the risk of extending the strike by asking the court to give Mr. Ritchie extensions so he could get the job done, he could not get the job done.

Mr. **Oberstar**. The gentleman's time has expired.

Mr. **Kolter**. Mr. Chairman, I have just one more question. Mr. Shapiro, has time lapsed or does Mr. Ritchie still have the opportunity to knock on your door to talk with you?

Mr. **Shapiro**. Any time.

Mr. **Kolter**. Your door is open?

Mr. Shapiro. Any time. He can talk to me any time. He can talk to my expert at any time. At any time, I am always available to him. I said it enough in court. I will say it here. The fact is, however, that if he wants to submit a competing plan, after the plan of reorganization has been filed and that will undoubtedly be in the next several weeks, I am sure that I will still be there trying to help Mr. Ritchie do so.

Mr. Kolter. Thank you.

Mr. Oberstar. We do have a vote in progress on the House floor, but there are some questions. One or two quick ones. I would like to bring the next panel up before the second call.

In determining operational viability have you as examiner asked the FAA their opinion as to whether the Eastern plan is realistic and viable from a safety or regulatory standpoint?

Mr. Shapiro. I have done this. I talked to the highest levels of the FAA and I asked the general counsel of the FAA to inform me, as examiner, whether or not there were any violations of FAA regulations post-strike. I was told about one incident that had occurred. I believe it was at Kennedy in which people, after having contracted out their maintenance, people had in violation of the regulations, done on-line maintenance at Kennedy, but that according to the FAA and what I have been told, there were no other violations that they knew about post-strike.

Mr. Oberstar. Excuse me, sir, but my question was whether the Eastern plan of operation, and I should include in that, also whether the Ritchie plan is viable from an operational and regulatory standpoint—you have not asked the FAA?

Mr. Shapiro. No, I do not believe it would be under their jurisdiction. The question of the viability of a plan would not normally, as I understand it, come under the FAA's jurisdiction. It might come under the Department of Transportation's jurisdiction, but not in my judgment the FAA.

Mr. Oberstar. Whether an operational plan from a safety, regulatory standpoint, that is the way I phrased the question.

Mr. Shapiro. I cannot answer this with any degree of certainty, but off the top of my head, I do not believe that they have the jurisdiction to deal with this kind plan that is originated in terms of a bankruptcy procedure.

Mr. Oberstar. I am thinking of such factors as training pilots, getting aircraft operational within the time frame under the standard regulatory authorities of the FAA.

Mr. Shapiro. They have to do that in any event. I mean, there is no way that anybody can fly aircraft or pilots can be trained and qualified without them being in both instances approved by the FAA.

Mr. Oberstar. It just occurs to me that the time frame within which retraining a pilot re-certification of aircraft and so forth takes place is important to determining viability.

Mr. Shapiro. I do not think there is any question about that.

Mr. Oberstar. There may be other questions we would have liked to ask. I think you have been most thorough and patient and responsive to the questions. It is apparent to me from your testimony and from the terms under which you are operating, under the bankruptcy law, that bankruptcy laws are rather rigid. Although you have some operational movement, it is a rather rigid to allow the flexibility one might have hoped or certainly one that I thought would be available under the circumstances.

That leaves a legislative question for Congress for the future as to how best to adjust that law to give people like you more flexibility to bring about a good result in a situation like this when we are operating on a matter within the public interest.

Mr. **Shapiro**. Thank you very much, sir.

Mr. **Oberstar**. I wish you well in your continued pursuit of a very difficult objective. You have made a good impression on all of us.

Mr. **Shapiro**. Thank you, sir.

[Mr. Shapiro's prepared statement follows:]

STATEMENT OF DAVID I. SHAPIRO, THE COURT-APPOINTED EXAMINER IN THE EASTERN AIR LINES BANKRUPTCY CASE

Mr. Chairman, Members of the Subcommittee, I appear before you today as the Court-appointed Examiner in the Eastern Air Lines bankruptcy case. I think it fair to say that it is highly unusual for a court-appointed official to testify before a Congressional committee about an ongoing court proceeding. I do so today with considerably mixed feelings and mindful that -- as the Committee obviously knows -- it would be inappropriate for me to discuss non-public details about the case. I accepted the Committee's invitation to appear today, however, because I believe that there are important public interests at stake and that Congress and the public should be as fully informed as possible about Eastern's status.

I have been in the private practice of law for 40 years, during which I have specialized in antitrust, labor relations, and other areas. When Judge Lifland appointed me as Examiner, on April 5 of this year, he publicly stated his concern that the private parties in the bankruptcy case were advancing only their own parochial interests. The Judge recognized the strong public interest in a competitive airline industry -- something made more difficult as the number of major domestic carriers dwindles -- and in preserving as many jobs as feasible. Judge Lifland's charter to me was to work with the parties towards a consensual resolution that would put the planes back into the air and the employees back to work.

With this objective, the Court directed the parties to move forward under my auspices on a number of tracks simultaneously. Two of these tracks, I believe, are of particular interest to this Committee.

The first track was to receive and to facilitate any potentially viable offers for the purchase of Eastern as a going concern. The second track was to assist and to expedite a plan of reorganization under which, if there were no sale, Eastern could still resume more complete operations.

Proceeding down both these tracks during the beginning of a bankruptcy case is not how the typical reorganization case moves. This is so because under the Bankruptcy Code the debtor maintains the exclusive right during the first 120 days to propose its own plan of reorganization, and the typical case does not have an examiner considering other opportunities. This case has been different. It has not been "bankruptcy as usual."

I have devoted a considerable amount of time to the first of the two tracks I have mentioned -- that is, to the effort to facilitate third-party offers. I have done so in the belief that, if the parties could agree to a sale of the company to a financially viable purchaser presenting an operationally viable plan for the airline, its striking employees would return to work, and Eastern could resume flying.

It was fundamental, however, that a serious purchaser would have to submit an operationally viable plan, because the process of restarting an airline -- the so-called "ramp-up" of an airline -- is enormously expensive; and every expert familiar with Eastern's tenuous financial condition agrees that there is one -- and only one -- opportunity to ramp-up Eastern. An ill-conceived or ill-managed ramp-up would hopelessly encumber Eastern with additional debts, prejudice the rights of creditors, and leave liquidation as the only alternative. Liquidation, of course, would lessen competition in the airline industry and result in the loss of many thousands of jobs.

It was likewise fundamental that any proposal would have to be financially viable in order to satisfy Eastern's creditors and to ensure that Eastern would not fail after six months or a year and return to bankruptcy in even worse condition -- again, a virtually certain candidate for liquidation.

Finally, it was also obvious that, to achieve a consensual resolution, a potential buyer of Eastern would have to offer fair consideration to Eastern's equity holder, Texas Air Corporation. It is beyond the scope of my duties to assess blame in the labor dispute between Eastern's management and its unions, and there is a wide range of opinions about Mr. Lorenzo and Texas Air. But Texas Air owns Eastern, and elemental due process requires that Texas Air receive fair compensation for its stock. Moreover, it was my hope that someone would offer Texas Air a deal that it could not refuse consistent with its fiduciary obligations to Eastern's creditors and Eastern's preferred stockholders.

As I have stated, I have spent a great deal of time over the past three months trying to identify and assist potential buyers. My highly experienced expert, Mr. Harry Kimbriel, who was recommended to me both by Eastern and by the pilots' union, assisted me in this process. I told each potential purchaser what I believed would be necessary to achieve the consent of the parties: an operationally viable plan, a financially viable plan, and fair consideration to Texas Air.

During this period Eastern Air Lines has been the most advertised piece of property in the United States. Yet no one has stepped forward with the basic, minimal components of a bona fide offer to buy and operate Eastern as a competitive carrier.

I have heard from a poet and an inventor, from a hotel magnate and a real estate investor, and from scores of other persons -- most of them well intentioned and many of them public-spirited, but none of them both willing and able to put a deal together. Unfortunately, the sad truth is that Eastern has such a significant debt problem that it is not a particularly inviting piece of property for investment.

The two groups that appeared most promising after the Ueberroth deal collapsed were headed by Mr. Joseph Ritchie (aided by Shearson Lehman Hutton) and by Mr. William Howard (in conjunction with Prudential-Bache). The Howard Group proposed at the outset what amounted to a leveraged buy-out; Mr. Ritchie offered $25 million. These proposals would have saddled the company with even more debt than currently exists. One of my law partners remarked that, if such deals were satisfactory, his five-year-old daughter could buy the company. They were not satisfactory.

Both the Ritchie Group and the Howard Group subsequently worked hard to raise equity to inject into the airline. And, again, I believe they were well motivated. But the principal source of funds the groups were able to tap in their attempts to reach a minimal $100 million level -- approximately a third of the estimated cost of ramp-up -- was through Eastern's unions; this created different problems.

For understandable political reasons, the unions were adamant that any resuscitated Eastern in which they would invest would have to be almost as large as the Eastern that went into bankruptcy -- that is, with something approaching 28,000 employees. As a consequence, despite repeated advice from experts that structural changes in Eastern were essential to revive the company, the operational plans presented by the Ritchie and Howard Groups contemplated no fundamental structural changes.

Such changes are necessary for the simple reason that Eastern cannot continue as a viable airline under the debt load that currently exists. Major assets have to be sold to reduce the enormous interest burden on the company, and the company needs to retrench to a competitively safe environment -- where it does not compete head-to-head with such giants as American and United -- until it is sufficiently healthy to regrow.

I suggested to the Ritchie and Howard Groups that, if they combined forces, they might be able to overcome their financial problems and to share other resources. (For example, late in the process the Ritchie Group still lacked the involvement of an experienced airline operator, like Mr. Howard.) And I spent some time and great effort trying to facilitate the groups' coming together. But for reasons that are extraneous to this hearing, they refused to come together. Moreover, despite repeated advice to do so, neither of them went to Eastern's owner and proposed a deal that either the owner would find inviting or the Court could deem to be so reasonable that Texas Air's refusal of it would be evidence of bad faith.

Upon my recommendations, and over Eastern's heated objections, the Court extended deadline after deadline to allow these groups to come up with something solid. I made these recommendations with the awareness that in the process the Court might be encouraging the striking unions to hold out against Eastern. The Court nevertheless resolved to explore every opportunity to allow third parties to purchase Eastern and to get it flying again.

At one time or another in this process, I have received loud complaints from every constituency -- from the creditors and Eastern that I was interfering with their prerogatives, and from the unions and potential suitors that I was not sensitive enough to their concerns and intentions. I like to think that the fact that I received complaints from each of the special interests in this case reflects that I have kept my eye on the greater public interest, as I was charged by the Court to do.

Finally, considerable time has also been spent analyzing the business plan which Eastern has proposed. As you undoubtedly are aware, that plan envisions a "downsized" Eastern -- one with only 17,000 employees, at least at the outset. I have publicly stated that my expert and I have preliminarily concluded that the plan is financially and operationally viable, with certain caveats -- such as Eastern's ability to recruit the pilots it needs and guarantees that Eastern will not upstream money or assets to Texas Air.

These past months have left me with the reluctant but firm conviction that only two practical alternatives remain in this case. The first is a reorganization plan premised on a smaller Eastern Air Lines; the second is liquidation.

I intend to use my energies to oppose liquidation and promote the best reorganization plan possible. To be sure, a "downsized" Eastern means the loss of a large number of jobs that existed in the pre-bankruptcy Eastern. But it is the opinion of Mr. Kimbriel and other experts that some substantial "downsizing" is necessary. It is my hope that Eastern's unions will come to accept this reality.

I sincerely regret I cannot paint a more optimistic picture for this Committee. But a bankrupt airline in the highly competitive, post-regulation, domestic airline industry is forced to make tough choices, whoever runs it, just as Congress is forced to make tough choices in the face of an enormous deficit. Some programs are cut so that others can flourish. The same truth holds here. Some jobs must be lost so that the majority can be saved and so that the opportunity for a strengthened Eastern to expand competitively in the future with a greater workforce can be preserved.

There is a ray of hope in the picture I have painted. This week I have been meeting with both the company and the pilots' union in an attempt to resolve their underlying labor dispute. These talks will continue over the July 4th weekend. And next week the talks will expand to include tandem but separate negotiations with the machinists and the flight attendants. With a little luck, with a willingness to compromise on all sides, and with a lot of prayer, we may yet settle these strikes and get this airline back into the air.

I thank the Chairman and the Members of the Subcommittee for this opportunity to provide an overview of these aspects of the bankruptcy case, and I welcome any questions you may have.

Mr. **Oberstar**. At this point, the Chair would like to call as our next witness, Mr. Phil Bakes, President and Chief Executive Officer of Eastern Air Lines with the announcement that we will now break for a motion to recommit with instructions which will be followed by final passage on the Foreign Assistance Authorization Bill. So we will have to break for roughly 20 minutes, unfortunately.

[Recess.]

Mr. **Oberstar**. The Subcommittee will come to order and we will resume the testimony with our next witness, Mr. Philip J. Bakes, Jr., President and Chief Executive Officer, Eastern Air Lines. Mr. Bakes, welcome. Thank you for your patience, and we will not have any further interruptions of votes, I am sure. So you may begin with your testimony. I have read yours as I have all the other statements thoroughly and would appreciate it if you would summarize your presentation. And we may precede some questions.

TESTIMONY OF MR. PHILIP J. BAKES, JR., PRESIDENT AND CHIEF EXECUTIVE OFFICER, EASTERN AIR LINES, INC.

Mr. **Bakes**. Thank you, Mr. Chairman. I will do that and obviously answer any questions the Committee may have.

Mr. **Oberstar**. Your testimony and that of all others will be included in full in the report, the prepared testimony.

Mr. **Bakes**. Thank you. I am pleased to be able to try to outline briefly our revitalization plan for Eastern Air Lines, Mr. Chairman, but to understand the current situation a little background is quite appropriate. Let me quickly just review a couple of the highlights of that.

Eastern is not new to losing money. Eastern has been losing money for many many years—for the last 20 years to be precise. And since deregulation has lost over $1.5 billion and during that period of time it took on an enormous amount of debt in order to fund those losses. Debt that was used to make payroll, to acquire aircraft, to upgrade facilities, and only for internal airline purposes.

The bankruptcy that we find ourselves in today is a bankruptcy that we did not want and we should not forget what the precipitating event was. The event was the strike that occurred by three of the principal unions of Eastern Air Lines in early March of this year; 90 percent of the Eastern union employees did not report to work. Another 12,000, some of whom were union and some of whom were not, did choose and want to come to work. And it is from that basic work force that we tried to rebuild the company.

But when that strike came, after two years in negotiations, that put us in a tremendous cash crunch situation. The company would have been out of cash very shortly and without bankruptcy we would not have an Eastern to discuss today, unfortunately.

The cruel irony of that strike or those strikes, is that during the negotiations and the two years of negotiations that led up to them, Eastern offered the unions some of the very guarantees that they rightfully insist upon and rightfully say are very important. We offered a guarantee to our pilots of a minimum fleet that would not go below the number of planes that we had in the fleet at the time.

We guaranteed that no pilots would be laid off. We guaranteed a minimum number of captains among our pilots which was the number of captains that were working at Eastern at the time in early March. And we proposed, in fact, that there would be future pay increases and did not even propose pay decreases to our pilot's union.

Let me also dispel the notion, if in fact, it needs any more dispelling after Mr. Shapiro's description of the Ueberroth deal in early days of bankruptcy process—the notion that we have not been responsive to trying to find a way, if feasible, to see the largest Eastern Air Lines possible fly and resume operations.

Texas Air which owns Eastern Air Lines is not just Frank Lorenzo. Texas Air has 30,000 shareholders and a board of directors and owns not only Eastern, but Continental and has others who share responsibilities. Texas Air in the early days of the bankruptcy, despite an analysis that says that the net worth on a liquidation value of Eastern Air Lines is close to a billion dollars, worked very hard, as did we, the management at Eastern, to put a deal together with Mr. Ueberroth which would pay the shareholders about half that price. We worked very hard to make it work. A lot of the parties worked hard and Mr. Shapiro, I think, has described well what made that fall apart.

After it fell apart we had to face reality. And the reality is that we had to deal with a company with the enormous debt it had; the unions who were still insisting they would never come back to work under this current ownership structure and this current management; a company which had now been virtually grounded for nearly two months, not just a few days; and therefore, routes which were quickly being taken over by competition in some areas, and frequent flyers who were moving out of our frequent flyer program and earning miles on others.

We wanted to put a plan together that would preserve as much of Eastern as possible. But we had to also protect a couple of other things. We had to design a company that was going to be restructured to provide industry leadership in operational performance which we have done on on-time performance very consistently for three months.

Provide competitive service. We had to revitalize a franchise, provide a work environment that is conducive to providing the best service. Weather a spool up cost estimate of $300 million in cash which is what Mr. Shapiro testified to. Repay ticket holders who were stranded when the unions chose to strike, suppliers and others the millions of dollars, many millions of dollars that they were owed, and do so in a way that they could be paid in cash quickly as we got out of bankruptcy. Make creditors whole, creditors who had provided billions of dollars to the company over the years to fund losses and to keep the company viable.

And do all this in a manner that did not produce an underlying grave risk of future failure to the detriment of obviously consumers, the communities we were serving, and of course the very employees that would be employed at the company. And to do that requires enormous financial resources. And there were no outside, I think quite obviously, sources for those enormous financial resources.

And the source of those financial resources to pay creditors and restart the airline was our plan to sell a substantial amount of assets to raise the capital, to raise the "venture capital" as we call it, for the restart of Eastern Air Lines.

But that selling of assets should be put into perspective. We are talking about selling $1.8 billion of assets with the total asset value on a market basis of the company as of March at about $6 billion, so less than a third of the assets of the company were to be sold.

The new Eastern that we put together will have 17,000 employees by the end of this year. It will generate an estimated $2.5 billion in annual revenues. The rebuilt airline will consist of initially approximately 157 aircraft. It will carry approximately in its first full year of operations about 23.5 million customers. It will serve 77 cities with over 800 flights a day.

That I submit to the Committee is clearly a major airline by any definition. We will be providing service to virtually every domestic destination we served prior to the strikes and prior to the most unfortunate reorganization process. But the difference, it will be a stronger and healthier company, a company free of the enormous crushing load of excessive debt, and therefore it will have a chance, and a darn good chance to succeed which is not something Eastern has had in literally the last 10 years.

I also want to say it has been said that we intend to get out of Miami or not serve Miami in a significant way. That is just not correct. Atlanta has always been our largest hub. It will again be our largest hub. But Miami will continue to be a very large center of operations for Eastern Air Lines, both flight operations, maintenance operations, and otherwise.

We will be the ninth largest airline in the United States. In size we will compare roughly to U.S. Air or Piedmont. By the end of this year, Eastern will be approximately 70 percent of the size of the pre-strike airline. And we are not talking about an airline that is just going to be. The airline I am describing is already becoming. It is already happening. Remarkable progress has already been made. Today there are 7,600 employees at Eastern Air Lines. Up from 1,500 right after the strike.

If our plan is to liquidate the company, we are going about it in a very very strange way. We are today providing 88 daily flights to 27 communities, and in just three days on July 2, this Sunday, we will be adding 226 daily additional flights. And in less than five weeks, we will be expanding again by another 50 percent of that.

Eastern is providing today also some of the lowest fares in the sky. In the environment of high fares, it has been discussed and commented on, we think it is a very good consumer offering.

Let me also say another thing. There is ample room, and I mean this very sincerely, for the unions at Eastern Air Lines and for the men and women who sit behind me now who are skeptical, bitter, and have undergone some tremendous hardship during this strike, and men and women who are not here, who are looking for other jobs or on the picket lines, or doing whatever they are doing, there is tremendous room for those people in this institution. We have begged and pleaded for the people to come back to work. I personally have gone on national TV begging and pleading. I have personally made phone calls, as other people have, asking people to come back to work, making ourselves available to try to explain the business plan, and get through this very difficult period.

We have also up to now felt the stiff arm of rejection from union leaders and the adamant statement that they have been making up until very recently, and I emphasize up until very recently, that they would never ever come back to work under this ownership and management structure. And we have had to take them at their word. We had no choice. But we continue to welcome them back.

While we are waiting, we have begun to hire and train new pilots, and we have hired over 700 pilots at Eastern to add to the approximately 300 who crossed the picket line and rejected the admonition of the union to strike. We are hiring very experienced people. It is in the record. I will be glad to answer any questions on it, but let me just make one point. That the highest average flying time of any pre-strike series of classes of new hired pilots at Eastern Air Lines was approximately 4,300 hours which is a very very high minimum time. The average hours of the pilots we are hiring post-strike have 5,700. And we are exceeding the minimum requirements the airlines have all over, including Eastern by a factor of four or five.

We continue to seek to negotiate in good faith with ALPA, with the Transport Workers Union, and the IAM. And in fact, there have been discussions as late as yesterday. I personally participated in discussions right here in Washington this week under Mr. Shapiro's not so gentle prodding.

During these few short months, we have also made pension payments of $117 million and we have applied to make an additional pension payment of $78 million in September, including making up for all the pension waivers we have had in the past of another $20 million.

Another important part of our plan is employee relations. I hope each of you will take the opportunity to fly Eastern and see what is going on with the 7,600 employees today. There is a very strong esprit de corps among these men and women who are bucking all odds to try to save an airline. They are enthusiastic. They are independent. But there is a feeling of mutual self-interest and most importantly, mutual support and mutual respect. And I can tell you that I am personally dedicated and the whole management team is to creating and doing the best we can to create an internal culture that sustains that feeling that is there today.

We will use every tool and resource available to us to do that.

We have announced that we will implement a meaningful profit-sharing plan for employees. There is enormous risk in taking a company through bankruptcy and restructuring, but there may also be upside, and we believe there is, and we think the men and women who are building it should share in it.

We have seen many so-called proposals to buy Eastern Air Lines. Mr. Chairman and the members of the Committee, I can tell you and I will be very brief because Mr. Shapiro has covered them well in terms of his perspective that they have run from the financially infeasible to the downright silly. Most would require Eastern to rapidly enter highly competitive markets in the weakest travel period of the year and burden the airline with substantial additional debt. In fact, Mr. Ritchie's latest proposal proposes it would be

$1 billion more debt on Eastern Air Lines than what our proposal has. $1 billion in additional debt.

All experts, except those being paid by Mr. Ritchie, have said that these proposals, competing proposals, are either confusing or likely to fail, or both. Mr. Ritchie has taken up the time of the court, the creditors, Eastern, and the employees for two months now. It is a tremendously expensive and counter-productive process in my view. We have objected vigorously to Mr. Shapiro and to the court for continuing it. Eastern is losing $1.7 million a day, and the only people profiting are the advisers and the lawyers and the lobbyists, and we have got to get on with rebuilding the company.

In our view the court and the examiner have gone too long with this, but that will be their determination. But we think it is unfair to consumers, to travel agents who need certainty at this time with Eastern Air Lines. And it is unfair to the 7,600 working men and women of the company who want certainty, many of whom have been trying to communicate that fact, while they are at work. I believe it is also unfair to the men and women behind me here who have come into this hearing room and the other striking employees. I think it is unfair because it gives them a cruel, false hope of a white knight, of a magic solution for Eastern Air Lines.

And unfortunately, there is no magic solution. It is a hard difficult restructure.

Under the control and supervision of the bankruptcy court process that has been described here and the bankruptcy court which does take in very vigorously notions of the public interest, as well, it should by the way, Eastern is implementing a sound plan which will enable our company to operate without the crush and burden of excessive debt and which for the first time in decades will make Eastern a strong, competitive and major airline serving the American public. And I suggest to you that that is in the public interest.

I am available for any questions, Mr. Chairman.

Mr. **Oberstar**. Thank you, Mr. Bakes. We appreciate your participation in the hearing. And the Chair will recognize the gentleman from Pennsylvania, Mr. Clinger, who has a time constraint.

Mr. **Clinger**. Thank you very much. Thank you, Mr. Bakes, for appearing before us and describing what the Eastern management proposes to do with the restructured airline. Obviously, there is some skepticism in some quarters about that plan. The thought that basically this is all being done as a subterfuge for ultimately liquidating the airline and getting as much as you can in liquidation and getting some of the creditors paid off and moving on. What kind of assurance can you give us that is not in fact what your bottom line objective is?

Mr. **Bakes**. Mr. Clinger, there is really three assurances, I guess. One is watch what we are doing, not only what we are saying. Watch what is happening with Eastern. The fact that we have brought back 6,100 employees in 90 days. The fact that we are proposing new schedules, putting them up in the air, going through the training, enormously expensive process of putting the airline back up in the air, providing new uniforms to our public contact employees, redesigning interiors of aircraft, increasing the money we are spending which is in our business plan on meal service, on redcoats meeting airplanes, and the whole panoply of customer service. Running and spending enormous amount of money and effort and time to do it to run the number one on time airline in the United States which we intend to stay at. This is no evidence of a company trying to liquidate. You would not put that kind of effort and time in if that was the case.

The second thing I would say is that we believe, we are in the airline business. I have heard Mr. Lorenzo's name bandied about here. The fact of the matter, Mr. Lorenzo's been in the airline business since the time he got out of school. His first job was as a financial analyst at Eastern Air Lines. The first company he got involved in as a principal was a company that had 3,000 employees and was on the verge of bankruptcy. And now under the Texas Air umbrella, there are about 60,000 employees, 17 years later.

The fact of the matter is that we are in the airline business. We are not in the liquidation business, and that is all we know and that is all we have done. We have made mistakes. We have done some things that make sense. And we got a lot of years to spend in this business.

The other thing I would say is that it is under the supervision, Mr. Clinger, of course, of the court. And the court has made absolutely clear that it does not, and does not intend to countenance a liquidation of this company. And it has really been the company, as well as with the court supporting it, putting pressure on those factions on the Creditor's Committee who just have a financial interest purely and might be very well served by a liquidation. And we are now negotiating a plan with the Creditor's Committee that I think we will have agreement on in a matter of days if not weeks that will not have a liquidation, will rebuild a substantial airline, and will get the support of the creditors.

Mr. CLINGER. We have talked a lot about critical mass and what do you really need to have to create a viable operational entity. The proposal is to sell basically $1.8 billion. Is that it? Or can we anticipate that you may sell off other assets down the road?

Mr. BAKES. No. Our plan is to sell what we estimated would be $1.8 billion about 90 days ago. We will probably end up selling fewer number of assets than we originally anticipated.

Mr. CLINGER. Fewer number or fewer dollar amount?

Mr. BAKES. No, a larger dollar amount, but fewer number. What has happened is the airline market for assets has been stronger than, I think, most people could have projected. The shuttle transactions is an example and some other transactions. So I can say to you that as it currently looks, we will probably sell fewer number of assets, fewer airplanes, for example, but end up with about or slightly higher dollar amount than we projected. And with that dollar amount, the sources of where that money goes is very important. About $550 million goes to get the company out of bankruptcy, meaning pay all past debts that have been missed during this period of time, pay about $70 million in cash to consumers who are holding tickets that were not good after that strike occurred, as well as a lot of suppliers that are out money, including $100 million to the pension fund.

And about $800 million will go to pay down debt over and above that which is normally scheduled, pre-paid debt, if you will. And approximately $500 million or more will be left over for cash resources. And an airline needs enormous cash resources going into this competitive environment. My point is none of that money is leaving the company, except to pay off creditors and consumers.

Mr. **Clinger**. One of the plans, as I recall, is that you propose to sell off some of the South American routes; is that correct?

Mr. **Bakes**. That is under discussion. That has not been done yet.

Mr. **Clinger**. Secretary Skinner has some reservations about this. What impact would the inability to sell off those routes have in your plan?

Mr. **Bakes**. The Department of Transportation has very extensive jurisdiction over any sale of international routes, as this Committee is very familiar with, and the DOT exercises it will continue to as the Secretary has made very clear, very close oversight of it.

If we go ahead with the transaction to sell the South American routes, we would only do so if we thought it was very important to the restructuring and survival of the company. And we would obviously have to take into consideration anti-trust considerations that would be there and public interest considerations.

I heard it mentioned earlier by Mr. Shapiro that there is about 900 employees associated with the South American routes. That is quite correct. We have not entertained any proposal for South American routes unless employees would be employed by the acquiring entity which is exactly the condition we put on Mr. Trump when we first negotiated with him, and he did take the employees in that enterprise.

Mr. **Clinger**. One final question. ALPA pilots recently requested Federal mediation. In their contract dispute with Eastern, what impact will that have on your plans to reorganize?

Mr. **Bakes**. Mr. Clinger, that is hard to say I really do not know. It is legally complicated. I do not pretend to know the answer to it. Mediation can often take a long long period of time. The ALPA contract was up over a year ago and mediation still did not even begin prior to the bankruptcy. But in terms of what impact it has, I think it is too early to tell. We will just have to see.

Mr. **Clinger**. Thank you, Mr. Bakes. Thank you, Mr. Chairman, for indulging me.

Mr. **Oberstar**. Mr. Bakes, the examiner, Mr. Shapiro, in response to questions and also on his own voluntarily in his testimony said it was the walk-away provision of the Ueberroth proposal that caused it to fail. My understanding was that it was a request for appointment of a trustee to oversee the Ueberroth deal that caused it to fail?

Mr. **Bakes**. I think, my perspective, Mr. Chairman, Mr. Shapiro I think was quite correct in his description of what happened. I have no quarrel with it at all. I would just add another dimension to it. And the other dimension is that although Mr. Shapiro for the obligations he had to fulfill insisted that a Ueberroth deal be structured so that there not be a walk-away by Mr. Ueberroth.

We to the contrary were willing to go forward with a deal that did have a walk-away with Mr. Ueberroth. And it was in that context that the trustee was insisted upon by certain parties to the negotiations, in particular the unions. We tried to solve that particular problem, the trustee problem, by proposing a couple of things in terms of interim control. That number one, there could not be any sell of assets during the interim period and any assets transaction—any transaction—out of the ordinary course of business would have a veto by Mr. Ueberroth.

That number two, Mr. Ueberroth could nominate members of the board of directors and join our current board, and I think we have some pretty distinguished members already, but he would add his.

Third, that he would be active in the management of the company during the interim period. In fact, I showed him where his office would be, and fourth, Mr. Shapiro would also have an office at the company during the interim period to try to solve some of the interim management things.

We were not, however, willing to go forward with a transaction that had total walk-away, but yet right when the deal was signed, we would have to give up total control of the company and management of the company before creditors are paid, before shareholders are paid. That we were not willing to do and that was what the effect of a trustee appointment would have done.

Mr. **Oberstar**. Was that particular provision insisted upon by the unions?

Mr. **Bakes**. Yes.

Mr. **Oberstar**. Your testimony indicated that you will need about 830 pilots. You used a couple of different figures in the course of your presentation, but my reading of the testimony indicates that you now have about 300 pilots who crossed the picket line. That means you will need 500 more pilots to meet your August schedules. You also further indicate that you had about 700 pilots hired. Does that mean that you are anticipating that some 500 pilots will complete training by August and be ready to fly?

Mr. **Bakes**. No, Mr. Chairman. The numbers, if I might just correct the numbers. We have a need by the end of the year for 1,700 active qualified pilots through the training and through initial operation experience. We have today approximately 430 or so that fit that category, consisting of approximately 300 that have crossed the picket line and been with the company for some time, and another 130 or so who have been through the training program and have been hired and are out flying. We have in addition to that several hundred in training and in the pipeline. What we will have for the August schedule we have published is enough pilots by far to fly that schedule.

We initially had projected that we would have about 70 hours a month of utilization from the pilots, and actually we are getting in mid-80 hours a month. Of course, the FAA requirement is nobody can fly over 100 hours a months. So we are still well below that. And that is why we will be able to fly the August schedule.

Mr. **Oberstar**. Has this new entity, Eastern Air Lines, been in touch with the FAA. Have you received approval of your training program?

Mr. **Bakes**. Yes.

Mr. **Oberstar**. Have they certified the pilots?

Mr. **Bakes**. Yes. I would characterize it a little differently. We have not only been in touch with the FAA, Mr. Chairman, it is a living arrangement. The FAA is very involved in the training program, and not only the training program and the design of it and the approval of the program, but the implementation of it. The

FAA itself has to date on three different occasions for each individual pilot that goes through the training, certify or test them or be present when they are being tested at three critical junctures during the training, the FAA inspectors themselves.

Mr. **Oberstar**. One of the key issues in this whole process, of course the matter of pilots, the numbers—I am going to have to think that over and revisit that issue later—but in addition to the personnel is the physical assets, the selling off of physical assets. Mr. Shapiro described the process that is somewhat more structured than we had anticipated or that we understood previously. Do you have to in order to sell an aircraft present a plan of sale and proposal to Mr. Shapiro to the examiner before you can go ahead with the sale of that or any other asset?

Mr. **Bakes**. We have to present a proposal and a motion and seek court permission. Not technically Mr. Shapiro's permission but court permission. In that process, all parties, Creditor's Committee, and I might point out that the three unions are official members of the Creditor's Committee, and so have not only access to material when it is presented in court, but in confidential Creditor Committee meetings where we have to go through proposed asset transaction.

But that is presented to court. All parties get to study it and Mr. Shapiro takes a position. He is not shy in taking a position on things.

Mr. **Oberstar**. He makes recommendations to the judge based on what you propose and submit? And it does not receive his approval, he makes recommendations and it is the judge who approves?

Mr. **Bakes**. That is correct.

Mr. **Oberstar**. It is a formalized process?

Mr. **Bakes**. That is correct.

Mr. **Oberstar**. I will suspend at this point and recognize Mr. Kolter.

Mr. **Kolter**. Thank you, Mr. Chairman. Mr. Bakes, you almost had me fooled. Really, I was reading your testimony here and it was quite convincing and then you came to that part, and I am going to be kind to you, I am going to call it fairy tale in which you stated that the pilot training program is so effective and they will be just as experienced as the pilots who are on strike. And let me read what you state here. You state that the you have 114 pilots that have completed their training. This training program consists of 45 days of training, 6 days of indoctrination, 10 days of classroom ground school, 5 days of cockpit ground school, one day of oral exams, 8 days of simulation training, one day of simulator flight checks, so on and so forth.

Now how in the world can you convince the flying American public, and we are grownups here today, the skies are safe with pilots who have that type of training?

Mr. **Bakes**. Mr. Kolter, that training is probably more extensive than the people out here received. We have added to our training. And the issue is the training number one, and the experience of the people being hired, number two, and the oversight of that process, number three. And I submit to you, Mr. Kolter, on all three scores, we are second to none in the industry on all three scores. The experience of the people that we are hiring, the average pilot and command time of the people we are hiring is over 2,300 hours. The average flight time is 5,700 hours. The average age of the people we are hiring is 39 years of age.

All of these parameters are far in excess in what our historical experience has been, and far in excess of what other airlines do. Secondly, in terms of our training, we have one of the best pilot training programs in the business. We have pioneered the notion of cockpit resource management and Line-oriented training, which is supposed to create environments of managing the resource in the cockpit environment. And if you look at the study that is done by NASA, by the National Transportation Safety Board, by the FAA, by Academics virtually every accident that has involved pilot error has been due to not experience or inexperience, it has been caused by failure to manage the resource properly, paying attention not to the major problem, but to minor mechanical difficulties which was not the major problem. I can go on.

So this training is not even required by the FAA. We are far in front of the industry on this. I am very proud of it. And third in terms of the FAA oversight, it is more vigorous and more intense than any airline is receiving. And perhaps properly so, and we welcome it.

Mr. Kolter. I would hope you could sell that to the American flying public.

Mr. Bakes. That is the challenge we have, Mr. Kolter.

Mr. Kolter. It is deeper than that. Because I have here a copy of a newspaper dated March 27, the Miami Herald, indicating that your airline seems to be bragging about the fact that ticket agents, your former attorneys are performing maintenance inspections on your aircraft.

Mr. Bakes. Mr. Kolter, that is just factually incorrect. I do not know what the article says, I can tell you what the reality is. And the reality is that we right now have about 1,000 people performing maintenance at Eastern Air Lines. About 700 of those are former Eastern and have been Eastern supervisors and management maintenance personnel. There are about 200 people working in the maintenance department who do not have prior maintenance experience. They are former management people. Some are former attorneys. Some are current attorneys. Some are out of marketing. And the things that they are doing are cleanup, running for parts, very routine kinds of things under the supervision of these very experienced people.

Mr. Kolter. You know in this article, sir, there is an article where a Mr. Kizer who is a former attorney with the FAA I might add.

Mr. Bakes. Yes.

Mr. Kolter. He seemed to have a little bit of problem. He evidently was using a mechanical tool, like a wrench and it fell, it dropped inside of a jet engine. And he was characterized as being very ill about that. Now if he were a real mechanic, that certainly would not have presented a problem to him. How can you justify having former white collar people doing mechanical work and telling the American public that the skies are safe by flying Eastern?

Mr. Bakes. Mr. Kolter, I would invite you to come down and see what is going on in the maintenance area.

Mr. **Kolter**. I would like to do that.

Mr. **Bakes**. We would love to have you.

Mr. **Kolter**. Perhaps, Mr. Chairman, the whole Committee ought to go down and investigate this.

Mr. **Bakes**. You are welcome at any time. [Applause.]

Mr. **Oberstar**. The gentleman from California, Mr. Bosco.

Mr. Bosco. Thank you, Mr. Chairman. Mr. Bakes, I noticed in your testimony that the plans for buying Eastern were both financially infeasible and downright silly. Given that you have not had all that much luck in making Eastern profitable and the last I read Continental has had seven straight quarters of losses, who is making the decisions in your operation as to what is financially feasible?

Mr. **Bakes**. In the first instance, Mr. Bosco, we are. We are making plans and recommendations. When I say that, it is the management team at the company and a very experienced and capable group. The vast majority of whom were at Eastern long before I arrived at Eastern and have tried mightily to make the company profitable, not only under this management but under Frank Borman, under Eddie Rickenbacher and others.

Mr. Bosco. I guess though what I am saying is since you have not successfully or profitably run an airline, what would cause either us or the American public or the bankruptcy court to believe that the glowing report you have given us today about the revitalized Eastern is ever going to come true, any more than the old Eastern or——

Mr. **Bakes**. I would answer that in two ways, Mr. Bosco. Number one, I have run a profitable airline. I was president of Continental Airlines and it was very profitable when I was president of that company. We took that company that was in bankruptcy out of bankruptcy. It was down to 4,000 employees and when I left that company, it was at 18,000 employees, and I was darn proud of the job we did. It was profitable. The employees earned money from profit sharing, and they earned stock in the company, and they made a lot of money on it.

The second thing I would say is that in addition to that, is that this is a process that is very well overseen by people other than us and other than the management. The Creditor's Committee have their experts, airline experts. The bankruptcy process has its own through Mr. Shapiro, and Mr. Kimbriel, the airline expert. And it is being looked at every day.

And the third, the ultimate judge, is going to be the American consumer. But it is not a lead pipe cinch. I do not think I gave a glowing report. It is a very risky proposition. This company needs and has had to have major surgery. It has been sick financially for a long long time. And it is not a lead pipe cinch, but we are working hard to do it, and I think we will be successful.

Mr. Bosco. May I ask you another question that does relate to the Government's liability here, as opposed to labor problems or anything else. But how are you doing on the pension funds? You alluded to paying back some element of the waivers that you had received. Are you up-to-date now or are you still behind on the payments?

Mr. **Bakes**. We are up-to-date on all payments that have been required to be made. We are not behind. We have had a previous waiver that is due to be repaid this fall of $19.9 million.

Mr. Bosco. Are you asking for any further waivers?

Mr. **Bakes**. No, we have proposed to the bankruptcy court to allow us to pay that as scheduled which is September 15. If the bankruptcy court determines that that should not be paid until we emerge from bankruptcy, we have filed a conditional permission with the IRS to allow us to pay it at the end of the bankruptcy. But we are asking to be able to pay it on time. In either event, it will be paid.

In addition, there is a $78 million payment due in September which we have also applied, for a total of approximately 100.

Mr. Bosco. So you are saying that of all the payments, you are liable for to your pension funds you paid them all? You have no liability. The Government is not exposed to any liability?

Mr. **Bakes**. There are future payments that will have to be made in subsequent years, and if Eastern does not survive, those would be in question.

Mr. Bosco. Back when we were considering the Presidential Emergency Board did you appeal to the Pension Benefit Guarantee Corporation to in turn lobby either the White House or the Department of Transportation against that idea in that it would perhaps expose the Government to more liability?

Mr. **Bakes**. Not to my knowledge.

Mr. Bosco. No one at Eastern did that?

Mr. **Bakes**. I said, not to my knowledge. It would have been, in my judgment, a very logical argument to make. Because I think that is a correct description of what the risks were at the time. But to my knowledge, I am not aware of any lobbying if there was.

Mr. Bosco. You are saying it would be logical to make the argument that a Presidential Emergency Board that would have lasted for about 30 days could have jeopardized your obligations in the pension plan, and yet the strike that has lasted for what is it over three months now?

Mr. **Bakes**. Mr. Bosco, our judgment was that a Presidential Emergency Board usually lasts much longer than 30 days, number one. Number two, we have been in negotiations with intense mediation for about two years, and there have been no solution. And number three, the company was losing more money per day, than it is losing after the strike. And our view was that it would put the company at greater risk, and people can disagree on that, but that was our judgment.

Mr. Bosco. May I ask one more question. Has former Secretary of Transportation, Burnley, advised Eastern Air Lines, Texas Air, or any of your people in any way related to the business of your airlines?

Mr. **Bakes**. No, nor in any other way.

Mr. Bosco. Thank you very much.

Mr. **Bakes**. Thank you.

Mr. **Oberstar**. I want to come back to the matter of pilots and how this airline is literally, as well as figuratively going to get off the ground. How many pilots are you going to need for your August schedule?

Mr. **Bakes**. Mr. Chairman, I do not, as I sit here know the exact number. I would estimate that we will need an average somewhere around 550 to 600, but I am guessing. I could obviously supply that data to you. I do not have it with me as I sit here today.

Mr. **Oberstar**. What I have pieced together in preparing for this hearing were some numbers from your testimony and from other fragmented information that you anticipated, that Eastern anticipated in having about 830 pilots to meet its projections for an August operation. It occurred to me that in order to get the necessary number of pilots by August, you would have to have a pretty sizable training program. But it also occurs to me that looking at the previously cited figures that only 40 percent of each class that you have brought in has successfully completed training, according to the numbers that we saw for the first five pilot training classes.

The question is, how then do you meet that schedule, number of aircrafts flying, the number of passengers, routes to be flown? How do you meet that number and match that with the number of pilots and the dropout rate in the training?

Mr. **Bakes**. Mr. Chairman, if those figures were correct, we would have some difficulty. But let me correct the figures. We originally had, in early April, made a projection that of so many pilots hired per month, per week, and how long the training process would work, how many flight simulation periods would be available to us, et cetera. It is a complicated process. And how many hours per month pilots would fly. Those are, of course, the variables. The attrition rate in terms of graduations is now at about 10 percent, not 40 percent. The first class that hired in many many weeks ago was—I think it was 33 or 35 was in the first class that started, and the graduation that occurred from that class was about 22. And in that class, two had been injured, two had dropped out for their own personal reasons, some had not made it through and flunked or let go, and some were in further training and graduated in subsequent weeks. But that was the first class and I think that is the figure that has been put about as projecting what the average attrition rate is. The attrition rate now is at about 10 percent.

Secondly, we will not have the 800 pilots by August. As I said it will be more like, and I am estimating at 550 to 600, but they will be flying more hours per month than we had estimated in April. They will be flying in the mid-80 hours per months, rather than in the high 60 hours per month. And with them flying the extra hours than what we had projected, we will be able to make our August schedule.

Mr. **Oberstar**. Getting accurate information is key to understanding what is happening and evaluating all the charges and counter-charges and determining what is happening in the public interest or how it is being effected. So those are definite numbers then? You will stand by those?

Mr. **Bakes**. No, Mr. Chairman, I told you that they are estimates.

Mr. **Oberstar**. If you would submit then specific data, so that we would had it on record.

Mr. **Bakes**. That is what I was going to say. I will submit complete data to the Committee.

[The following was received from Mr. Bakes:]

More than 325 pilots have crossed the picket lines, 260 pilots have completed training and about 680 are currently enrolled in the program. Under Eastern's plan, the company will need a total of 1,700 pilots to operate its projected schedules by December or early 1990. We have not had any trouble attracting pilot trainees. Thousands of applications have been received from qualified pilots. In fact, the pilot trainees are the best qualified, most experienced in the airline's history. They average 18 years in the cockpit, 5,700 flight hours and 2,700 hours of pilot-in-command time. Eastern had projected that more pilots would have completed training by August than have actually done so. This is not because of a lack of qualified pilots for the program, but because of our insistence, and that of the FAA, that the training be driven by safety concerns alone rather than efforts to meet business plan projections. Eastern is building for the long-run stability of the company; decisions on pilot training will not be driven by short-run expectancies. It is Eastern's intention to increase our flights from the present 225 flights daily to 350 on August 1 and 390 on August 15. As I stated, these schedules will be met with the existing pilots flying more hours per month than we had estimated in April. In addition, Eastern has arranged to lease 5 aircraft and crew from Continental Airlines for a limited number of these flights. Additional increases will be implemented in September and during the fall. We fully expect to reach our target of 800 daily flights within four to six weeks of our original estimate of late December. These operating factors have been reviewed by the creditors committee and they have indicated no objection.

Mr. **Oberstar**. Further on that same point, after the crash in 1987 of a Continental Airlines flight in Denver, the FAA issued a recommendation that airlines schedule their crews so that the flight would not be operated by an inexperienced pilot and an inexperienced first officer. Now you are going to have a very large number of replacement pilots operating this system when you get into your August schedule. What steps are being taken to assure that at least one crew member has substantial experience to comply with that FAA recommendation?

Mr. **Bakes**. Mr. Chairman, that is a very very good question and one we have thought about at length, and in fact, the FAA recommendations, we are going to exceed those recommendations in terms of the margins and are working and are due to submit a proposed policy that we intend to file to the FAA very very shortly, and will be working with the FAA. And it will consist of a number of things.

It will consist of making sure that crews that are paired together, there is not two inexperienced people paired together. And when I say inexperienced, it is important to point out, we do not mean inexperienced pilots, we mean people that do not have a lot of hours on that particular equipment as a captain in that equipment. These are very experienced pilots, and many of whom who have flown this type of equipment before. But they have not flown Eastern equipment. We have a number of former people from Braniff, from Transtar and other airlines, private airlines that fly the same kind of equipment that we do.

But in addition to making sure that inexperienced people are not paired is also using very high minimums in terms of clearance to land in certain weather conditions until the experience is even higher. Such that the situation of that terrible tragedy in Denver several years ago, if in fact it was caused by inexperience, in that particular crew, we would not in the policies we are putting forward, they would not be allowed to take off even in that weather with that same amount of experience in that equipment that that particular crew had.

Mr. **Oberstar**. I am sure it may be unavoidable to have two relatively inexperienced people in the cockpit and that is where you are having some very high minimums. You have got to take those additional precautionary steps.

Mr. **Bakes**. It is very critical. I could not agree with you more. We take that very seriously.

Mr. **Oberstar**. As I read your testimony last night and reread it again this morning on page 6, your proposal to sell or your plan I should say, to sell about $1.8 billion out of the $6 billion assets, and the plan that you have now described, I have concluded, and I want your assessment if that is an accurate conclusion that Eastern is not up for sale? There is no buyer who could come in now and put together a viable plan to acquire Eastern?

Mr. **Bakes**. Eastern is not for sale, Mr. Chairman. Mr. Shapiro, I think, also described fairly accurately to perhaps at times to our consternation that even though we do not have Eastern for sale, apparently he and the court does under the right circumstances in their view. Any sale proposal that is made, we would have an obligation to consider. We do have shareholders. We do have a board of directors. But our board of directors has concluded that it is not for sale. That it is vastly unlikely for there to be any viable proposition presented to the board to acquire Eastern in a way that is financially sound. And that in the interest of the investors and all the stockholders in the company, it is best for us to go forward with our rebuilding and revitalizing plan for the company.

Mr. **Oberstar**. Are you planning to sell off your Caribbean and South American routes?

Mr. **Bakes**. We are in discussions on our South American routes and some Caribbean routes.

Mr. **Oberstar**. Is that because they are not profitable or because you need the money to finance the planned operations of the company?

Mr. **Bakes**. Both of those reasons. They are not profitable and the money, if the right transaction—the facts are they are not profitable and have not been for some time. And let me add one other reason, is that if a transaction can be done that makes sense financially and operationally, we would go forward in part because we think it is very important for the resources and focus of the airline to be kind of undiluted, if you will.

We have a tremendous competitive challenge to rebuild the Atlanta hub and rebuild the Northeast to Florida service, rebuild Miami service. And that is going to take financial and management resources and marketing resources. And we think it is a mistake for the airline to be spread too thinly. But we have not sold those routes as yet. I am very forthright with you, we are in discussions, and if those discussions come to fruition in a way we think makes business sense for the entity and for the airline going forward, we would propose such a thing to the Bankruptcy Court and to the Department of Transportation for their consideration.

Mr. **Oberstar**. It is your company. You know it better than anyone outside the operation, but the airline financial analysts with whom I have discussed this situation over the past weeks assign rather high values to those Caribbean and South American routes. I will give you this opportunity to submit to the Committee some documentation that supports your view that they are not profitable or cannot be operated profitably.

Mr. **Bakes**. I think both of those are consistent. I will submit that information. We think they have values as well, but it is also true that they are not profitable for Eastern Air Lines and have not been for some time.

Mr. **Oberstar**. This downsized airline that Mr. Lorenzo is proposing to operate, both in his public and other descriptions of it and what we have heard of it from the examiner and your testimony indicates that somewhere in the range of 157 aircrafts will be operating and it seems to be an entity that will be at the lower limits of critical mass. A fancy word that everybody is using these days to operate this new entity successfully. If it is not as successful as your earlier projections and that number does not seem to be sufficient, then where do you go?

Mr. **Bakes**. That is a good question.

Mr. **Oberstar**. Do you have further assets to sell off?

Mr. **Bakes**. There are additional assets at Eastern, but no that is not what we have. Let me say one thing that I think is important to understand in the bankruptcy process. In order to get a plan confirmed which is approved, the word for approved in the bankruptcy process, there has to be a showing that the plan and the operating company after the bankruptcy is a feasible company. And what that standard essentially is is that there is not an undue risk that the creditors and those investing in the company will not have their notes repaid. It is a financial test.

In a sense, it is a proxy for a prediction of success. And what we will have in that process is creditors who are going to be asked to take notes, reinstated notes. Not cash upon liquidation. They are not going to agree to such a plan unless they think the company is feasible. Boeing, for example, is one of those creditors. Boeing has just completed an extensive study on our plan and have found it to be extremely feasible and think it is going to work. It was only after they completed that study after several weeks did they get into serious negotiations with us, as them being a member of the Creditor's Committee of whether or not they would accept some plan that would reinstate some of their old notes, as opposed to pay them all cash.

So we are going to have a process that will test its feasibility by a number of experts and people who really have a stake in it being successful. That is one test. Number two, we will have had some operating experience over several months. It will probably be late in the year, at least in the fall, before a plan could ever be confirmed. So we will have several months of operating experience to see if it works.

In terms of the critical mass question, let me say two things. One, the 157 planned airplanes is the initial size airline at the end of December. We have not said the next step which is the implication that some people have is that we are never ever going to acquire another aircraft. That it will be frozen in time for the next 10 years. That is obviously not the case.

What we would see is a company, because we are projecting a profitable company in 1990. We are projecting a profitable company in 1991 with a restructured balance sheet. And in fact, we are literally right now in discussions about options and possibilities of having the ability to acquire new aircraft as well as used aircraft over and above the 157.

And the other thing I would say, I think we are going to end up with a plan that is somewhat higher than 157 aircraft.

Mr. **Oberstar**. What would be the average age of the aircraft in that fleet?

Mr. **Bakes**. The average age prior to the restructuring that we are going through now was about 15 years and the average age afterwards would be about 15 years. There will be no material change in the average age.

Mr. **Oberstar**. If another party or if the Ritchie group as harking back to Mr. Shapiro's testimony came back with the Ueberroth deal without the walk-away provision, according to your previous testimony, that plan would be rejected by Mr. Lorenzo. There then would be little likelihood the Bankruptcy Court could force Mr. Lorenzo to accept a deal?

Mr. **Bakes**. No, I think it is a little more complicated than that, Mr. Chairman. And that is that if Mr. Ritchie came back with a plan that is the kinds of plans, and he has had many plans.

Mr. **Oberstar**. That is not what I said. What I said was the Ueberroth plan, as described by Mr. Shapiro.

Mr. **Bakes**. No, the Ueberroth plan in our view from an operational point of view and I think in the view of Mr. Kimbriel, the expert for the examiner, is no longer a feasible plan. That was a plan early in the bankruptcy before American had entered many of the Miami markets. Before consumers had deserted as they will. Eastern has been on the ground. I do not think the airline could be built back to anything like the size that Mr. Ueberroth was proposing. I think at the time, it had a good shot. But I do not think it any longer does.

Mr. **Oberstar**. So there is no conceivable proposal now that could be offered?

Mr. **Bakes**. Mr. Chairman, we have shareholders. If somebody came in and offered $2 billion in cash to Eastern Air Lines, I assume our board of directors would stand up and take notice. And I am not trying to be facetious. What I am trying to do is make a projection and a prediction and a business judgment that we have made after spending a long time at this and seeing the various proposals that have come in.

We do not believe—we believe two things. We do not believe there would be any proposal that is financially feasible for investors or for the ongoing company. That is what we believe. And number two, we believe the process of shopping the company, whether voluntarily or involuntarily, is very detrimental to the very interests that I suspect this Committee is interested in, and that is a certain environment for consumers, for employees and get on with the rebuilding.

Mr. **Oberstar**. The net result of all this is that Mr. Lorenzo will have won personally.

Mr. **Bakes**. I do not agree with that. I do not think there are any winners.

Mr. **Oberstar**. He will have the airline. He will have used the bankruptcy process to his advantage. He will be divested of unions, at least at the outset, and he will be operating a new restructured airline.

Mr. **Bakes**. Mr. Chairman, with all due respect, I do not agree with the characterization in this sense. I do not believe there is any winners in the crises that has occurred to Eastern Air Lines. I think there is only a series of less harmful choices than other harmful options. And there has been enormous damage done. In human terms, the damage has been enormous. In financial terms, it has been enormous. And there is no way to change that. There is no way to fully restore that. So in that sense, I do not think anybody is a winner here.

In terms of Mr. Lorenzo personally being a winner, he does not own Eastern Air Lines. He does not own Texas Air. There are 30,000 shareholders of Texas Air. He is the chairman and chief executive of Texas Air. And he has fiduciary obligations as I do, as others do. And with the plan we are putting forward, we think it is the best chance to have the fewest losers.

Mr. **Oberstar**. Certainly you may characterize it that way, but we certainly have not heard from any shareholders other than Mr. Lorenzo. I do not think the public has either. I am just saying that in the final analysis, it is Mr. Lorenzo who has called the shots. It is Mr. Lorenzo who has masterminded it. It has been very brilliantly done, but he has used the protection of the law through to his advantage, and he walks away, he has the whole thing in his bag. No one else does.

Mr. **Bakes**. Mr. Chairman, one of the purposes of bankruptcy is to try to reorganize and save a company. And that is what we are trying to do. And in that sense, if we are able to be a part of that process, it is a victory. But I think it is a victory in the public interest.

Mr. **Oberstar**. Thank you very much for your presentation and your comments. I appreciate your being with us.

Mr. **Kolter**. Mr. Chairman, may I ask just one question here, sir? Not really a question, but I wish Mr. Bakes would do something for the Committee here. Mr. Bakes, I do not mean to be beating up on you on the issue of pilots and pilot training and safety, but you mentioned, I believe, that the people you are hiring have 2,300 hours of training; is that not correct?

Mr. **Bakes**. No, actual pilot and command experience flying as captains of aircraft.

Mr. **Kolter**. 2,300?

Mr. **Bakes**. That is their average. The flying time, the average is 5,700 hours.

Mr. **Kolter**. It seems to me I read something in Sunday's Post where you were advertising for 1,200 hours. That is a vast difference.

Mr. **Bakes**. Mr. Kolter, that is the minimum requirement for Eastern, and that is about what other airlines require as a minimum requirement. What I am saying is the people we are hiring are exceeding their minimum requirements by a factor of four.

Mr. **Kolter**. Are you also aware of the fact that you have a former employee who formerly worked with Gulf Air, who voluntarily left Eastern's training program on June 16 of this year due to a question of flight crew safety and qualifications? Are you aware of that Mr. Bakes?

Mr. **Bakes**. I am aware of his interview that he gave in the Boston Globe. I would be glad to describe this gentleman. He came into training and lied on his application. He actually had had an FAA violation for drinking when flying, and he was had a serious FAA violation that he lied on his application. Our background checks which go on right before they are hired and during the process of the early couple weeks of training discovered that. And he was about to be fired, so he quit. He is getting paid $2,400 a month now by ALPA to hold press conferences to talk about his tremendous concern for safety. And that is the fact.

Mr. **Kolter**. So you are aware of the fact, sir, that he claims under a sworn statement here that he recognized a former roommate of his from Gulf Air who was terminated because he failed to pass the check rides on a Boeing 747 as a first officer, yet he is being trained by Eastern on June 12 as a captain? Is not that kind of scary?

Mr. **Bakes**. Mr. Kolter, I have not seen that statement. I would submit to you that the facts I just gave you are correct. That I have serious doubts about this gentleman's credibility in light of that, and we will investigate those charges as well.

Mr. **Kolter**. I would appreciate that, sir.

Mr. **Bakes**. We will get back to you on it.

Mr. **Kolter**. Thank you.

Mr. **Oberstar**. When you submit the data I asked for on the number of pilots, if you would clarify another matter that is still a factual matter, at least appears to be a dispute with numbers. In the May statement about the bid for pilots in August, the number cited was 837. Clarify that for us and if there is a document that was issued stating that number, submit that. And if the number is different, explain why.

Mr. **Bakes**. I can do that briefly now, Mr. Chairman.

Mr. **Oberstar**. I really would like to get on with the other witnesses.

Mr. **Bakes**. I will submit that to you.

Mr. **Oberstar**. Thank you. Mr. Bosco?

Mr. **Bosco**. Mr. Chairman, I beg your indulgence for one second. I have a question though that I think is relevant. Mr. Bakes, are you going to submit your reorganization plan by the 7th or 8th of July which we understand is the 120-day period?

Mr. **Bakes**. I believe we will come very close to that. We are in discussion with the creditors now trying to wrap up the final points.

Mr. **Bosco**. Thank you.

Mr. **Oberstar**. Thank you very much again.

Mr. **Bakes**. Thank you, Mr. Chairman.

[Mr. Bakes' prepared statement follows:]

TESTIMONY

OF

PHIL BAKES

PRESIDENT & CHIEF EXECUTIVE OFFICER

EASTERN AIR LINES, INC.

BEFORE THE

HOUSE SUBCOMMITTEE ON AVIATION

HOUSE COMMITTEE ON PUBLIC WORKS AND TRANSPORTATION

June 29, 1989

I am pleased to be here today to outline the Eastern Plan for the reorganization and revitalization of Eastern Airlines. As I understand it, this hearing has been called to:

(1) Ascertain whether the bankruptcy court is or should be taking into consideration public interest issues, including the effects on consumers;

(2) Explore Eastern's plans for expanding service in the upcoming months; and

(3) Look at other proposals presented for Eastern's reorganization.

To understand the current situation and the Eastern bankruptcy, it is very important to review Eastern's problems leading up to the bankruptcy. Let me review that quickly.

First, Eastern had been losing money for two decades and was facing a $2.4 billion dollar debt. Since January 1, 1980, Eastern had lost over $1.5 billion before gains from the sales of assets and tax benefits. During this period, Eastern had net losses of over $1 billion, while the remainder of the industry had a net income of approximately $2 billion. The substantial profits earned by the rest of the industry, while Eastern suffered enormous losses, allowed other companies to make significant expansions into Eastern's markets, thereby exacerbating Eastern's financial problems.

Eastern's losses had been largely funded by debt financing. As of September 30, 1988, Eastern's debt and capitalized lease obligations totalled approximately $2.4 billion, its annual debt service was approximately $560 million in 1987 and approximately $575 million in 1988. Eastern's ability to use its resources for product enhancement was further hampered by the labor costs and by the unprecedented and expensive takeover campaign waged against it by its unions. Thus, Eastern's combination of interest expense and labor costs, as a percentage of operating revenue, has been the highest in the industry.

Second, the bankruptcy was caused by the union's decision to strike. As of March 4, approximately 90% of Eastern's union employees did not report to work. This meant that 90% of Eastern's revenues were being lost largely because most of Eastern's pilots did not report to work. This strike came after nearly 2 years of negotiations with Eastern's two principal unions. And, the cruel irony is that, during those negotiations, Eastern offered the unions the very guarantees this Committee seems to want and the unions now profess are so important to them. We offered a guarantee of a minimum fleet size of no less than 226 aircraft (the number of aircraft we had at the time) and therefore that level of service. We agreed contractually to protect the existing jobs and to prevent lay-offs and furloughs, including guaranteeing the number of captain positions for the pilots. We proposed that there would be no pay cuts for pilots and, in fact, future pay increases. These proposals were rejected and the strike commenced causing the Eastern bankruptcy.

Third, we were simply running out of cash. It was with the utmost reluctance that Eastern filed bankruptcy under the protection of Chapter 11. It was not possible to avoid bankruptcy, unless the Government chose to provide massive subsidies. Had we not done so there would be no Eastern Airlines today. There would be no opportunity to rebuild and revitalize Eastern and there would be no hearing today on the future of Eastern Airlines.

Fourth, let me also dispel the notion that, having filed bankruptcy, we were not responsive to trying to find a way to put a larger Eastern back in the air while it was still possible to do so promptly. Texas Air and its 30,000 shareholders agreed reluctantly to give up its valuable position in order to accomplish this in the proposed sale to the Peter Ueberroth group. We worked very hard with Peter Ueberroth and others. Unfortunately, despite the fact that all parties wanted to see the airline sold, it was not possible because of the union insistence that before the deal was closed, before the owners were paid, before Eastern came out of bankruptcy and while Eastern took all of the risks, that Eastern management and directors be removed in favor of an unknown trustee who had no stake in the outcome. The deal fell apart over that.

Fifth, we had to face reality. And the reality was that we had to deal with a company with an enormous debt; unions who insisted that they would never come back to work for the company despite our requests to negotiate; a company which had been by now virtually grounded for nearly two months; routes which were quickly being taken over by the competition; and frequent flyers who were moving out of our frequent flying programs and into those of the competition.

The truth of the matter was we simply could not pretend that March 4 never happened. Any airline facing this reality needs serious and delicate rehabilitation, not unlike a star football player who has torn up his knee. Some day that player may be every bit as great as the day he was injured. But in the interim, there will have to be major surgery, and a slow, carefully monitored recovery program. No matter how much that player or his fans may want him to return next week, that simply will be impossible.

Neither we nor anyone else can ignore the injury to Eastern. In this condition, if Eastern tried to return to the playing field immediately, it would be permanently crippled just as surely as the football player who would try foolishly to play on an injured knee. So, we had to develop a business plan that faced reality and we did so.

We wanted a plan which would preserve and protect Eastern as a major operating airline able to:

(1) provide industry leadership in operating performance;

(2) provide competitive service;

(3) revitalize its franchise;

(4) provide a work environment that is conducive to providing the best service anywhere;

(5) weather the spool up costs of at least $300 million in cash;

(6) repay ticket holders, suppliers and others the millions of dollars owed to them in cash;

(7) make creditors whole, creditors who provided billions of dollars earlier to keep Eastern afloat; and

(8) do all of this in a manner that did not produce an underlying risk of future failure to the detriment of consumers, communities and all of Eastern's stakeholders.

To do that, to accomplish that ambitious and worthy mandate was not feasible without access to massive financial assets. While we would be happy to listen to any ideas Congress might have about government subsidy, that does not seem a likely prospect. So, we have proposed, in order to finance the new Eastern and assure its success, the sale of approximately $1.8 billion out of the $6 billion in total assets. This will allow Eastern to rebuild its operations, pay off Chapter 11 liabilities and most importantly, pay off nearly $1 billion of Eastern's $2.4 billion dollar debt. In addition it will provide a substantial cash balance of over several hundred million dollars by the end of the year. This will allow the new Eastern to become a sound and secure organization thereby reversing nearly a decade of financial crisis and losses at the company which began long before the purchase of Eastern Airlines by Texas Air.

This recovery plan was presented to the creditors in April and presented to the staff of the House Public Works Committee in May. Under the plan, which has been successfully implemented to date, the "new" Eastern will have over 17,000 employees and will generate an estimated $2.5 billion in annual revenues. The rebuilt airline will consist of 157 narrow and wide-body aircraft which will carry an estimated 23.5 million passengers a year. It will serve 77 cities with over 800 flights per day.

Eastern will be providing service to virtually every domestic city that it served prior to the strike and because Eastern will be stronger and healthier than it ever was in the past, it will provide better competition than it did in the past. In communities where Eastern is not going back with as big a presence as it had, new competition has been introduced. The Trump Shuttle is already competing with Pan Am. Our current contract with Midway will bring new competition to Philadelphia and the East Coast. To the extent that Eastern does not provide service to international points that it has served, they will be markets which are limited-entry and Eastern will be replaced by a carrier which meets the public interest standard.

The new Eastern will be the ninth-largest airline in the U.S. and will be able to effectively compete with all of the major carriers in its markets. In size, it will compare roughly to USAir and Piedmont. By the end of this year, Eastern will be approximately 70% of the pre-strike airline.

Remarkable progress has already been made. Immediately after the strike we had approximately 1500 employees. Today there are 7600 employees and Eastern is providing 88 daily flights to 27 communities. In just three days, we will be providing 226 daily flights and there will be another expansion in less than five weeks for 390 system-wide daily operations. The August expansion will bring us halfway to our goal of rebuilding to a full schedule of the "new" Eastern by December. Further, Eastern is providing some of the lowest fares in the sky. Eastern's new low fares represent tremendous overall potential savings to the consumer and they have met with high public acceptance.

There is ample room for the unions at Eastern. We have begged and pleaded the striking employees to return to work. We have told the Airline Pilots Association (ALPA), the International Association of Machinists (IAM) and the Transport Workers Union (TWU) that we want them back, that we are prepared and eager to bargain over back to work issues. But, we have felt the stiff arm of rejection, the position the unions have taken that they will not negotiate with us but only with a new owner and new management of their choice. We have had to take them at their word. Nevertheless, we continue to welcome back the nearly 300 pilots who have crossed their own union's picket line to save their airline. We have also begun to hire and train new pilots. We have hired over 700 pilots and have in place the applicants and the training ability to complete the hiring and training of the remaining 700 pilots needed to restore Eastern Airlines as a major carrier. We have received over 4,024 applications for pilot positions of which 2,647 meet Eastern standards. Eastern minimum standards require at least 1,200 average flying hours and 200 pilot in command hours. These qualified applicants have on average 4,890 flying hours and 2,478 pilot in command hours. Further, they average 37 years of age and are experienced and mature individuals. In fact, if the current ALPA Master Executive Committee (MEC) were to be hired today, six of then would not meet these standards. The first 13 classes of 733 pilots have already begun and

131 pilots have completed their training. This training program consists of 45 days of training. It includes 6 days of indoctrination, 10 days of classroom ground school, 5 days of cockpit ground school, 1 day of oral exams, 8 days of simulator training, 1 day of simulator flight check, 4 days of familiarization flying, 2 days of cockpit resource management and 8 days of initial supervised operating flight experience.

Nevertheless, we continue to seek to negotiate in good faith with ALPA. And, in fact, there were discussions as late as yesterday. I personally participated in those discussions. We earnestly hope that our striking pilots will join Eastern in making it the kind of airline we know it can be.

During these few short months, we have also made pension payments of $117.1 million by March and in September will make additional payments subject to Court approval of $78 million and a 3rd installment of $19.9 million for a 1985 waiver.

Another important part of this plan is employee relations. I hope each of you will take the opportunity to fly on Eastern because you will find that the current Eastern employees are enthusiastic about maintaining and building a strong, independent and competitive service.

We are dedicated to creating an internal culture of sound employee relations at Eastern. Eastern has had two decades of bitter conflict in this area. We will use every tool, technique and resource at our command to build on the current esprit de corp and commitment to service. Our challenge, which we are determined to meet, is to continue with the strong nucleus we have currently and build a cohesive work force dedicated to meeting customer needs. We see that one of the primary goals of management is to lead and to support all of our employees in their efforts to serve customers.

We have announced that we will implement a meaningful profit sharing program for all employees than ensures that the benefits of a more cost effective Eastern are enjoyed directly by all of Eastern's employees.

I continue to hear the assertion that somehow our plan is simply a guise for total liquidation. Nothing could be further from the truth. Our efforts to date and those planned for the future are aimed directly at preventing a liquidation of Eastern Airlines. We would not have spent the money on hiring and training pilots, we would not have reinstituted service, we would not have brought back our non-contract employees, if we intended to liquidate this company. These actions have been taken to rebuild Eastern and for that purpose alone.

We know that this plan will work because it is already working. What Eastern, its employees and the traveling public need now is certainty. Continued uncertainty about the future of the company including pursuing the sale option of the proponents of this hearing will only delay and jeopardize the future of Eastern Airlines.

We have seen many so-called proposals to buy Eastern Air Lines, Inc. They run from financially infeasible to downright silly. Most would require Eastern to rapidly enter highly competitive markets, during the slowest travel period of the year, burden the airline with substantial additional debt and put creditors at high risk, including consumers and ticket buyers. The various proposals Mr. Ritchie has made fit that description perfectly. All experts, except those being paid by Mr. Ritchie, have found his operating plan both confusing and likely to fail.

Nevertheless, the Bankruptcy process has been burdened by allowing these competing proposals to be made, amended, re-made, and considered again and again over the vigorous and continuing objections of Eastern. The Examiner appointed by the Bankruptcy Judge has continued to meet with and thereby encourage a host of would be suitors, including Mr. Ritchie, whose ever changing proposals continue to surface. His plan, too, would require additional debt for Eastern and would require enormous risks attendant with restarting the airline too quickly. Further, according to Mr. Kupersmith, the financial advisor for ALPA, Mr. Ritchie has yet to obtain the financing for this proposal. On June 24, Mr. Kupersmith said that "Shearson-Lehman indicated that some time in the next several weeks they hope to be able to report back meaningful progress with respect to the commitments for the financing requirements to purchase the airline."

Mr. Ritchie has taken up the time of the court, the creditors, Eastern and the employees for nearly two months now. This is tremendously expensive and counterproductive for all parties. The hours, days and now weeks devoted to responding to Mr. Ritchie's constant interference is costing millions and diverting attention from rehabilitating our airline. Eastern is losing $1.7 million per day during this process. The only people profiting from all of this are the lawyers, the lobbyists and the financial advisors.

In our view, the Court and the Examiner should have stopped this bidding process weeks ago. Continuing the process is unfair because it produces uncertainty and nothing else. It is unfair to consumers, it is unfair to travel agents, it is unfair to the working men and women at Eastern -- 7600 of them who are working mightily to rebuild Eastern but who are constantly concerned that it will be taken out from under them. And, it is unfair to many of those Eastern employees who still remain on strike. They too must face the choice of returning to work or going a different way. Yet, the false promises of a white knight keep them in paralyzed state.

Now, because the court has left this process in limbo, this group is turning to Congress and to the media to effectuate what is essentially a hostile takeover, or better yet, a confiscation if you will, because unlike a hostile takeover, in this case the Directors have firmly rejected Mr. Ritchie's overtures.

This is America and so, therefore, Mr. Ritchie has an absolute right to make any offer he sees fit for the purchase of Eastern Air Lines, Inc. And of course, the owners have the right to decline to accept such an offer. And they have. Mr. Ritchie's efforts to cloak himself in the robes of the public interest can't change that result. And, they are particularly perverse when Eastern is implementing a sound plan which will enable the company to operate without the crushing burden of excessive debt or overhead and which, for the first time in decades, will make Eastern a strong, competitive, major airline serving the American public.

Mr. **Oberstar**. Our next witness is Mr. John Peterpaul, Vice President for Transportation of the International Association of Machinists.

TESTIMONY OF JOHN F. PETERPAUL, VICE PRESIDENT—TRANSPORTATION, INTERNATIONAL ASSOCIATION OF MACHINISTS AND AEROSPACE WORKERS, ACCOMPANIED BY JOSEPH GUERRIERI, JR., ATTORNEY, GUERRIERI, EDMOND AND JAMES, P.C., WASHINGTON, DC

Mr. **Peterpaul**. Thank you, Mr. Chairman. You are the Committee with all the action, that is why. Thank you very much, Mr. Chairman, I have submitted my written statement and then I will try to sum this up as briefly as I can. My name is John Peterpaul. I am Vice President of Transportation for the International Association of Machinists and Aerospace Workers, and have held that elected position since December of 1973. Our organization represents approximately 800,000 members in various industries throughout the Nation. At the present time, we represent approximately 95,000 employees in the airline industry including 8,500 employees on Eastern Air Lines. However, prior to Mr. Lorenzo's acquisition of Eastern Air Lines in 1986, there were 13,500 IAM members employed by that airline.

Mr. Chairman, before I get into summarizing the statement, you asked Mr. Ritchie the difference. Between his plan and basically Mr. Lorenzo's. There was one answer. He gave you several. There was one that was probably the most cogent that was missing. But the most important was that Mr. Ritchie can have access to 20,000 skilled employees tomorrow. Mr. Lorenzo does not have that available to him.

What is ironic about all that comparison between plans too, Mr. Chairman, is that you made reference to the Ueberroth deal. It is funny, the image that has been projected here in this hearing room about these various deals, but the Ueberroth deal was forced upon the unions by our very aggressive examiner. And it was acceptable at that time to the examiner, but here two months later, Mr. Chairman, there is the Ritchie deal. There is no question, financially it is far superior to the Ueberroth deal but it is unacceptable. Very ironic.

My personal opinion is that the court and the examiner have made any third party deal totally out of reach of anybody.

Mr. Chairman, I think I would like to take a few minutes to review how we got here, to lay some foundation because it was less than just four months ago I testified before this Subcommittee in favor of legislation which would provide the creation of a Presidential Emergency Board. At that time, I described how the IAM had made every effort to reach an agreement with Eastern in order to avoid a strike, including agreeing to binding arbitration which Eastern rejected. Subsequently, the National Mediation Board recommended that an Emergency Board be appointed to facilitate a settlement. We fully supported that recommendation and preserved the status quo. Again, Eastern vehemently opposed the NMB's recommendation. However, in a radical departure from every other past Administration in the White House, Republican and Democratic alike, President Bush refused to follow the recommendation of the National Mediation Board.

However, Secretary of Transportation Skinner candidly revealed before this Committee that he had been misled by Frank Lorenzo who had assured the Administration that he would fly over the heads of the picketing employees. Mr. Lorenzo also convinced the Administration and others that the appointment of a Presidential Emergency Board would cause him to file for Chapter 11 bankruptcy protection. We argued that if an emergency board was not appointed Mr. Lorenzo would again abuse the bankruptcy laws in an effort to break the strike.

Thus, the Railway Labor Act's 30-day cooling-off period was allowed to expire and on March 4, the strike that Eastern has been trying to provoke for more than a year began. Several days after the strike commenced, the unions worst fears were realized—Eastern Air Lines filed for bankruptcy by enlisting the aid of a bankruptcy court. Mr. Lorenzo for the second time in five years used the Bankruptcy Code to once again circumvent his obligations under the Railway Labor Act.

The extent to which Mr. Lorenzo has been allowed to manipulate the bankruptcy system is reflected in how he managed to file his petition in New York when Eastern Air Lines is headquartered in Miami, Florida. In anticipation of Eastern's bankruptcy, Mr. Lorenzo incorporated a small subsidiary, the Ionosphere Clubs in New York. On March 9, he filed a bankruptcy petition for this company and six minutes later, six minutes later, filed Eastern's petition as a related case. He thus piggy-backed Eastern, a company that is 2,000 times larger than the Ionosphere Clubs into a form that is widely accepted as a debtor's haven.

Unfortunately, this jurisdiction's reputation for favoring the debtor has proven all too true. Judge Burton R. Lifland, the judge assigned to this case, has regularly minimized the concerns of the employees and their representatives as and I quote, as he said it many times, "parochial interests," as if the workers that have labored for this company for so many years have less dignity than the corporate interests and should be pushed aside and ignored. Judge Lifland has now apparently embraced the view that what is good for Frank Lorenzo is good for the Nation. I submit that the bankruptcy court and the examiner have been seduced by the forces of darkness.

I will tell you what factually happened in that Ueberroth deal. On April 6, Mr. Lorenzo announced that he reached an agreement with Mr. Ueberroth to purchase the airline. However, the deal left Mr. Lorenzo free to back out after the employees had returned to work. Thus, possibly breaking our strike. Mr. Shapiro as he said here, fully guaranteed us, and I will quote from him again, "that Mr. Lorenzo is history on this property, and that the bankruptcy court would appoint a trustee if we reached an agreement with Mr. Ueberroth." The examiner assured us that by the appointment of a trustee the Ueberroth deal could not be abrogated and used as a strike-breaking weapon by Mr. Lorenzo. It was his assurance that made it all possible.

Following round the clock negotiations, historic agreements were reached early Monday morning, April 10 that would have provided the new owner with $1.25 billion in concessions from the employees over the next five years. And let us keep in mind that it is approximately the same amount that had been contributed to Eastern Air Lines by the same group of employees over the past several years. Labor proved at that time that it could make concessions to a management team that it would place trust in. Indeed on Monday morning, all parties including former Secretary of Defense Carlucci, who was selected by the examiner and consultation with the court to be the trustee, traveled to New York to await Judge Lifland's approval for the Ueberroth purchase and the appointment of Mr. Carlucci as trustee.

However, it quickly became apparent that over the weekend the judge was faced with a firestorm of opposition from Mr. Lorenzo's counsel that he could not resist. The judge after seeking but failing to get Mr. Lorenzo's consent to a trustee, sent Mr. Carlucci home. It was not for the reasons, in my belief that were stated here. In fact, Mr. Zorenski, Mr. Lorenzo's lawyer, said quite plainly that they told the judge that it was Lorenzo's airline. No trustee was acceptable to Mr. Lorenzo as long as Mr. Lorenzo was the debtor in possession. Thus, Mr. Lorenzo again prevailed, I believe, over the interest of the public, the creditors and the employees.

As a layman to the bankruptcy procedures, it is also my understanding that the court can appoint a trustee to put together its own reorganization plan, because that was the question that was asked by several Congressmen during the course of these hearings today. If the trustee is appointed he can put together a reorganization plan that does not need the approval of the debtor.

So through actions of the court, there is no question that the Ritchie plan could be a viable alternative to Frank Lorenzo's reorganization plan or liquidation. In any event, Mr. Shapiro then with a great deal of fanfare, began an investigation of fraudulent transactions engaged in by Mr. Lorenzo which we claim are over a billion dollars, and I am talking about pre-strike.

Upon his initial review of the most basic facts, Mr. Shapiro was able to conclude that Texas Air and Jet Capital's control over Continental and Eastern created a conflict of interest, I believe as quoted by Congressman Jones of Georgia earlier today. But in any event, the examiner promised a full investigation in the report to the court. However, that investigation has now been stalled at Eastern's request. The likelihood is that the examiner, having embraced the Lorenzo plan, will make no findings until after Eastern's plan of reorganization is approved. Thus, I feel that any ultimate finding that Mr. Lorenzo looted Eastern Air Lines may be rendered meaningless in the future.

Indeed, the examiner has neither taken nor scheduled a single deposition or called a single witness. Instead, he is making every effort in public statements and in private negotiations to break the strike. I know I feel both as professionally and personally that the men and women of Eastern have been betrayed. We expected it from Mr. Lorenzo, but not from the courts, the jurisdiction that is supposed to be established to protect the people.

Since Mr. Shapiro's announcement to the court blindsiding the Ritchie proposal which you heard about today, he and Judge Lifland have embarked on a crusade on behalf of Mr. Lorenzo and his business plan which every expert we have heard says cannot work irrespective of what you heard here today. Even Mr. Bakes in one quorum said that the Eastern plan is not incompatible with probable liquidation. Yet Mr. Shapiro has on numerous occasions stated, and I will quote him, "I believe in Lorenzo's plan more than Lorenzo does." Mr. Shapiro has supported and Judge Lifland has approved every request by Eastern to sell assets, including the Shuttle, numerous aircraft, gates and slots at various airports, totally almost a billion of dollars as of today.

This court, I do not think, has seen a sale of assets that it does not like. The velocity of this process is like panzer divisions over Poland. However, the court has yet to be presented with a formal plan of reorganization as required by the Bankruptcy Code. Yet everything around is attempted to be sold off. Mr. Lorenzo desperately needs to break our strike to achieve his goal of flying a drastically reduced airline while he liquidates.

Once again, the court and the examiner are assisting Mr. Lorenzo in accomplishing this goal. Upon the urging of Mr. Shapiro, the court has ordered the pilots into round the clock negotiations with Eastern and the transparent attempt to force the pilots to cross the IAM picket lines. However, acts in the contract with the IAM, the strike will still continue. We are frankly sickened by the fact that we no longer can obtain fair and impartial treatment from the examiner or from Judge Lifland.

We have attempted to the best of our ability to closely monitor Eastern's maintenance situation, especially as it attempts to put more planes in the air over the next several months. What we have learned and what I have to believe are very very reliable resources is that Eastern's maintenance program is in utter shambles. Eastern is woefully understaffed in virtually every maintenance area, and the mechanics they do have are predominantly either unskilled mechanics' helpers or people who are right out of training school.

Clyde Kizer, Vice President of Engineering and Maintenance of the Air Transport Association recently testified that it takes approximately two to three years of formal on the job training to achieve full productivity from a recently schooled mechanic.

I will illustrate a few examples of Eastern's maintenance crises. While Eastern's July schedule calls for the equivalent of about 65 aircraft, they plan to utilize 107 in order to postpone required maintenance as much as possible. If they actually attempt to fly their August schedule which calls for the equivalent of 95 aircraft, they will almost certainly run out of spare aircraft that are operationally fit to fly. Eastern has a critical shortage of mechanics.

The simple fact is Eastern's schedule will not operate in August as was stated here with, not only the pilots, but with the mechanical work force they have. The severity of Eastern's maintenance problems is demonstrated by its reliance upon secretaries, reservation clerks, and sales managers to perform critical maintenance work, including the most important seat checks.

A newspaper report included quotes from these workers in which they proclaim their newly discovered ability to repair aircraft. For example, an attorney stated, "after 30 years as an aviation lawyer, I am finally getting my hands on greasy parts." A sales manager confided, "I did not even know how to use a ratchet or a screw driver three weeks ago." Obviously our safety concerns predated the strike, but have grown now to the point that we believe Eastern's certification should be pulled. We are not crying wolf, we are sounding the alarm. And we pray that it will be heard.

Finally, even when Eastern's management has had qualified mechanics to perform the work as it did prior to the strike, they resorted to falsifying maintenance documents. An FAA investigation at Kennedy Airport recently revealed that supervisors regularly signed worksheet falsely indicating that essential maintenance had in fact been performed. As a result of the investigation, Eastern Air Lines last month surrendered its repair station certificate. Remember that, Mr. Chairman, we just discussed that two days ago right in this very room. And we have a violator of the process right here in the United States, and we were talking about foreign countries. Ironic, is it not?

On June 23, 1989, the FAA issued another report in which it determined that Eastern's maintenance systems in Miami and Atlanta failed to make needed repairs to malfunctioning aircraft, even after receiving repeated complaints from pilots. The documents on which the FAA based this conclusion include records of airplanes repaired after the strike commenced which are dated as recently as May 29, 1989. The FAA has initiated another investigation into the maintenance practices at LaGuardia Airport which is again prompted by reports of management requiring foreman to falsify documents.

Mr. **Peterpaul**. There are a lot of situations. We heard about the pilots and their training which I am sure they will cover. But let me just tell you one thing, Mr. Chairman, that I can go qualify for the school for the flight training at Eastern Air Lines right now. I have a commercial pilot's license and $1,200 that was referenced here. The biggest piece of equipment I ever flown was a single engine Bonanza. Even though I am a mechanic and I have taxied them, I would be scared to death of getting involved in a DC-9 or 727, after I have had months or years of training experience and hours of flying. Yet, these are the qualifications and some of that have appeared in articles in the Boston Globe and some of these other newspapers about where Eastern has gone to pick pilots to enter these schools. But I will back off of that because I am sure they make their own case.

Mr. Lorenzo's ongoing liquidation of this airline, while its staffing and safety standards deteriorate, I think, guarantee the demise and maybe the ultimate disappearance of Eastern Air Lines if something drastic does not happen. Another critical motivating force behind Mr. Lorenzo's sham business plan is the desire to escape from Eastern's $750 million unfunded pension liabilities, Mr. Bosco, the question you asked,—That is what is standing out there—$750 million in unfunded liabilities. That does not include the $100 million they are looking for waivers on right now. It is obvious that the fund over the years has been underfunded. There is no question about it in order to generate that kind of debt.

Nevertheless in view of all this, the PBGC (Pension Benefit Guaranty Corporation), has taken no action whatsoever to ensure that the benefits of thousands of retirees and the future of the

PBGC itself are not put in jeopardy. Even the court, the bankruptcy court has not fully addressed this critical issue as of this date.

Mr. Chairman, in conclusion, let me just say that since Mr. Lorenzo took over Eastern Air Lines in late 1986, he systematically looted this once proud carrier for the benefit of Texas Air and its other airline subsidiaries, Continental. I think the record is replete with evidence that we put on numerous occasions before this Committee that Eastern has been used as a spare parts airline for nonunion Continental. In spite of his amply documented destruction of Eastern as a major competitive force in the airline industry, Mr. Lorenzo is receiving significant assistance from the judiciary in the Executive Branch to further his ultimate goal, the complete liquidation of Eastern Air Lines.

Thus, we have a public policy dilemma of major proportions in my opinion. The Executive Branch has the authority and the obligation to foster airline competition, but has been deeply embarrassed in hopes to save face by ignoring the public interest. The judiciary through Judge Lifland has embraced Mr. Lorenzo and has forsaken the public interest by dispatching the examiner to break our strike.

Mr. Chairman, it is time once again, I believe, for Congress to act. Only Congressional intervention can save this airline. The bankruptcy system does not have the public nor workers at interest. It is designed as a haven for Mr. Lorenzo and for people like him to circumvent their obligations to the workers and the traveling public.

We stand prepared to assist you and your staff in devising the solution to the crises through your oversight of the Department of Transportation or any future legislation. I thank you very much for your patience and indulgence, Mr. Chairman.

Mr. **Oberstar**. Thank you very much, Mr. Peterpaul. You presented very weighty testimony. I read through it last night very carefully. There is a great deal more information in your prepared document than you actually delivered. It is a very comprehensive statement of the case and very thoughtfully delivered. It is apparent to me that the bankruptcy law itself is an impediment to the resolution of this particular dispute, and I think, declaring an impediment in any future case in which there may be airline financial difficulties.

While the bankruptcy law as it relates to railroads makes a very broad provision for the public interest to be satisfied, and of course administering bankruptcy law, airlines are not specifically covered. So there is a great deal less latitude for the court and for the examiner to operate. Although the examiner seems to have done more than the law apparently gives him authority to do.

But I think the first point of attack has to be or a major point has to be changing the bankruptcy law to add this almost identical language for airlines as now exists for railroads, and I was not aware of that before we got into preparation for this hearing or as we got into the hearing itself, and that is going to be an objective of mine.

Everything else about airlines is regulated in the public interest. Bankruptcy is not which is very curious. There is no more regulated—except for the nuclear power industry, probably—no more heavily regulated industry than airlines by the Federal Government, and rightly so because of the unique public interest in the airways and in the people who are served by the airlines. That is the first step that we have to take.

Secondly, had our bill been enacted, and a Presidential Emergency Board appointed, I think we would not have gone the 21 days provided in that legislation. I think there would have been a resolution which whether machinists or the pilots or the flight attendants would have liked or not, there would have been a deal on the table and you would have had to accept it because there was support of the Presidential Emergency Board and Eastern would be operating today.

All we heard was this stuff about we are going to lose $1.7 million a day while that Presidential Emergency Board is in effect and they have been losing $1.7 million ever since without the Board. Operation of that law would have meant that we would have had Eastern in its full array operating. Regrettably we do not.

You indicated that Mr. Shapiro ordered the pilots into a round the clock negotiations. Are those negotiations still going on?

Mr. **Peterpaul.** The pilots will be testifying next. I do not know exactly what the status is. I think they have started their meetings, Mr. Chairman. Henry Duffy is testifying next and he will be able to answer that.

If I may comment, Mr. Chairman, I think in your comments you hit it right on the head. The first words out of our mouth would have been modification of the law like we have in the railroad situation. Why not put the airlines under similar type of legislation, especially since we feel the majority of the problems that we have been confronted with have occurred as a result of deregulation. They have come about over the last dozen years because of this type of activity. There was not the foresight injected into that deregulation legislation to take care of these situations. What we have seen happening in the industry is not over yet.

The entrepreneurs, the money merchants and everybody injecting themselves into the process of this, I guess, is it the glory industry that they look at. Everybody tells me it is a fledgling industry. Eastern Air Lines was the first major airline we represented, and that was back into the late 1930's, 1938. I mean, how long is it going to be a fledgling industry. It has been 50 years, but we have heard that as an excuse for all of these inadequacies or things going wrong, and we refuse to accept that. Because 50 years has gone by the way side now and anybody that is 50 years old should have grown up.

Mr. **Oberstar.** You also raised a very interesting point in referring Eastern's heavy maintenance schedule, indicating that, parallel with that maintenance schedule, Eastern plans to sell additional aircraft to Continental. And that of the 11, Eastern plans to sell at least five which require D checks. Are they trying to dump their costly aircraft? That is costly in terms of repair schedule or maintenance schedules and get them off their hands to somebody else, so that what is left in the fleet is less costly to maintain?

Mr. **Peterpaul.** Not to be facetious, Mr. Chairman, but they are apt to dump their junk any place that they can. I can only base this on the information that we received, but they have, and we quote a figure, I think, like 30 aircraft that are inoperable. I think there are very many many more than 30 aircraft that are probably inoperable because they have not had the people to make any repairs, especially in the back shops on parts that go on the airplane. The easiest way to service an airplane is to take a part off one airplane and put it on another to get the airplane operational.

I cannot understand for the life of me why they are selling airplanes that are due for D check to Continental. They would sell better aircraft and less, it all depends on what type of aircraft they are. If they are 727, 200 series or if they are the better type of aircraft, they will stand to get off a plane that amount of money that is required in-house to do those D checks to keep those airplanes. The greatest commodity that Eastern Air Lines has is the wide body airplanes, the 757's. When we see those going on the block, we get distressed because there is the heavy market place for them. Those airplanes are bringing in the used market more dollars than they are off the assembly line, and look at the waiting period for obtaining those new aircraft.

So we get a little distressed with that. Of course we sit on the Creditor's Committee, come to think about it—at least confidentiality we are not supposed to talk about it. But for public information, the value of those airplanes is well known and it is advertised all over. We resist the sale of any assets. We want to keep this airline intact as much as we can. Mr. Ritchie started a month ago to try to make a purchase. He wanted the airline for what it was at that time. Mr. Ritchie is not going to go away. He will be here tomorrow for what airline there is. What we could hold intact

Let me comment on another thing, Mr. Chairman, because I have been to a lot of hearings, but there have been some impressions made at this hearing today that were not lies, but such falsehoods like I never heard before. For instance the union proposed that there be 28,000 people go back to this New Airline because that is how many went on strike. We made no such demand whatsoever. What we did was we sat down with potential purchasers. We devised a business plan, a viable business plan, that is all we were interested in. A viable business plan with the finances to support it. Whatever that plan generated as far as employees was going to have to be acceptable to us. Because do not forget, what the purchaser was buying was what was left. And as the bankruptcy process was going on, there was less and less.

We never demanded that there be 28,000 employees. We never demanded any employee. We said whatever the purchaser thinks that it takes to operate this airline and make it viable, that is what it is. In the Ritchie plan, the last one that was put on the table, it was 22,000. But let me tell you what was told to us. What was told to us by the examiner at 4 o'clock in the morning at the Drake Hotel, was, if you want to buy Eastern Air Lines, you have got to have a 17,000 employee Eastern Air Lines.

We said, what are you talking about? What is that? Well, that is what Mr. Lorenzo proposes. He wants a 17,000 man airline. You have got to have a 17,000. Man and woman airline, excuse me. We said, that is preposterous. We have to build a business plan around 17,000, that is stupid. We get a viable business plan and then with

50 employees into the business plan, whatever that takes. If it is 20, whatever it is.

But with Ritchie, we have the mentality. We have the support forces that if we did come back maybe with only 26, 24, or 22, we have got the ambition and the fortitude to build it to 28. Not what we think Lorenzo is doing, starting out at 17 and preparing for nothing but a controlled liquidation which he controls and puts it right down the tubes ultimately. Because every professional that is associated with this, except for a couple--you know, Mr. Chairman, in this area of professional investment bankers and the lawyers associated with the bankruptcy courts and the large investment banks, whatever you want to pay for, that is what you get.

It is very simple. I am sorry to go overboard, Mr. Chairman, but we are in a touchy and a very sensitive area that—then I have had to sit here a dozen hours today and listen to some of this stuff had me on the edge of my seat.

Mr. **Oberstar**. I can understand that fully well. I understand how deeply you feel about your members and about this carrier.

Mr. **Peterpaul**. Very deeply, Mr. Chairman.

Mr. **Oberstar**. And about all of the injustices that have gone on, some of which we heard about in our Investigations and Oversight Subcommittee last year.

The Chair recognizes the gentleman from California, Mr. Bosco.

Mr. **Bosco**. Thank you, Mr. Chairman. Thank you, Mr. Peterpaul, for your testimony. I do not have a question, but your testimony has prompted me to make a comment and perhaps address a question to the Chair. And that is that I think the similarity between the request that Mr. Lorenzo has made and the actions that the bankruptcy court has taken has caused me to wonder if it is not appropriate for our Committee to address this question of business plans. We have had an interest in this before Mr. Lorenzo put the airline in bankruptcy. It is perfectly appropriate for us to continue our interest, and I think that there is enough doubt about how this process works as to how these plans are analyzed. That I would like to ask the Chair if it would be possible if we requested a copy of each of the remaining plans and whatever information the court feels is comfortable in its own decision to grant us.

And then ask the Department of Transportation and perhaps other groups that the Chairman might feel could professionally analyze those plans to do an independent analysis of it for us.

Mr. **Oberstar**. Is the gentleman referring to the plans that have been submitted to the bankruptcy examiner, Mr. Shapiro?

Mr. **Bosco**. Yes.

Mr. **Oberstar**. We will attempt to obtain those. I cannot tell you right off hand because I do not know what the procedure is for making those public. But that is a valid point, and the staff will be directed to and make the appropriate inquiries for that.

Mr. **Bosco**. I think it would help our Committee's understanding to have an independent analysis of those plans, so that we would know in what perspective a lot of what we have heard today.

Mr. **Peterpaul**. If I may, Mr. Chairman, and let me just say this that I know that the organizations involved, the IAM, the ALPA, TWU, we have financial advisers we think that are so superior in this field as far as being straightforward because they analyze these things for us. We could provide all of the assistance, all the analogy between us with our advisers that we could possibly supply the Committee. Anything the Committee would need.

Mr. **Oberstar**. Thank you.

Mr. **Peterpaul**. Another thing, Mr. Chairman, let me just say this. I appreciate your efforts with how many times now we have come before you regarding Eastern Air Lines. You must be almost like a ruptured duck because it has been my third or fourth time pushing away to achieve and protect the interest of the employees, and the interest of this Committee and the feeling that you have had for it and the understanding that you have had for the problem has been very astronomical.

And we want to thank you on behalf of our organization, on behalf of the strikers for the grasp that the Committee does have in what is going on and for sitting there constantly and listening to us beat and beat and beat on Eastern Air Lines head. But believe us, they are evil creatures and deserve everything that we are saying about them and I wish we could just give them what they deserve in other fashions and forms.

Mr. **Oberstar**. Thank you for your kind comments. One does develop iron pants in this business. Within the confines of the bankruptcy law are there in your judgment any steps the examiner or the judge can take to encourage or to force Mr. Lorenzo to sell the company to an outside investor? I think it is pretty obvious that he does not want to.

Mr. **Peterpaul**. It is my understanding of the law, Mr. Chairman, that if the court appointed a trustee, the trustee then can formulate a reorganization plan without the approval of the debtor in possession, and the court can approve that. In other words, a case scenario, the court could appoint a trustee and he could sit down with anybody, including Mr. Ritchie, draft up a reorganization plan, and include Mr. Ritchie in it in this structure and submit it to the court for approval, as long as it came from the trustee. It is my understanding that you have got to have a trustee. That is why Eastern does not want a trustee because something like that might happen.

Mr. **Oberstar**. The bankruptcy law really is a very blunt instrument and it does not have quite as much flexibility or authority as it seems to me it ought to have to adequately reflect the public interest. We will pursue remedies.

Mr. **Peterpaul**. We will encourage you, Mr. Chairman, all the way.

Mr. **Oberstar**. Thank you.

Mr. **Peterpaul**. Thank you very much.

[Mr. Peterpaul's prepared statement follows:]

STATEMENT OF

JOHN F. PETERPAUL

VICE-PRESIDENT - TRANSPORTATION

INTERNATIONAL ASSOCIATION OF MACHINISTS

AND AEROSPACE WORKERS

BEFORE THE SUBCOMMITTEE ON AVIATION,

COMMITTEE ON PUBLIC WORKS & TRANSPORTATION

UNITED STATES HOUSE OF REPRESENTATIVES

JUNE 29, 1989

STATEMENT OF
JOHN F. PETERPAUL
VICE-PRESIDENT - TRANSPORTATION
INTERNATIONAL ASSOCIATION OF MACHINISTS
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BEFORE THE SUBCOMMITTEE ON AVIATION,
COMMITTEE ON PUBLIC WORKS & TRANSPORTATION
UNITED STATES HOUSE OF REPRESENTATIVES
JUNE 29, 1989

My name is John F. Peterpaul. I am Vice President for Transportation of the International Association of Machinists and Aerospace Workers (IAM) and have held that elective position since December 1, 1973. The IAM represents approximately 800,000 employees in various industries throughout the nation. At the present time, the IAM represents approximately 95,000 employees in a variety of crafts and classes employees in the airline industry including 8,500 employees on Eautern Airlines. Prior to Mr. Lorenzo's acquisition of Eastern Airlines in 1986 there were 13,500 IAM members employed by that airline.

I would like to begin my testimony by thanking Chairman Oberstar and all members of the committee for providing the IAM with this opportunity to tell the employees side of this tragic story. This is a story of a long struggle with the head of the Texas Air empire, Frank Lorenzo. Since his acquisition of Eastern Lorenzo has been committed to dismantling the airline, upstreaming its most valuable assets to its parent corporation Texas Air and to its favored non-union carrier Continental. Mr. Lorenzo has been hell bent on destroying labor unions on his only unionized carrier, Eastern, even if it means destroying the airline in the process.

Less than four months ago I testified before this subcommittee in favor of legislation which would provide for the creation of a Presidential Emergency Board. At that time I described how the IAM had made every effort to reach an agreement with Eastern in order to avoid a strike. In early February of this year the National Mediation Board proffered arbitration as a means of resolving the dispute. Although the IAM took the unprecedented step of agreeing to arbitration to avoid a strike, Eastern flatly rejected it. Subsequently, the NMB recommended that a Presidential Emergency Fact Finding Board be appointed to facilitate a settlement. The appointment of such a Board would require that the parties preserve the status quo during the deliberations. The IAM fully supported the NMB's recommendation while again Eastern vehemently opposed it. However, in a radical departure from every other past Administration, Republican and Democrat alike, President Bush refused to follow the recommendation of the Mediation Board. Before this committee Secretary of Transportation Skinner candidly revealed that he had been misled by Frank Lorenzo who had assured the Administration that he would fly over the heads of his picketing employees. He also convinced the Administration and others that the appointment of a Presidential Emergency Board would cause him to file for Chapter 11 bankruptcy protection. We argued that if an emergency board was not appointed Mr. Lorenzo would again abuse the bankruptcy laws in an effort to break the strike. Thus, the Railway Labor Act's thirty day cooling-off period was allowed to expire and, on March 4, 1989, the strike that Eastern had been trying to provoke for more than a year, began. As you know, the IAM testified in support of this Subcommittee's Emergency Board legislation. In stark contrast, Eastern remained adamant in its opposition to any attempt, legislative or otherwise, to end this dispute.

Several days after the strike commenced, the unions worst fears were realized - Eastern Airlines filed for bankruptcy. By enlisting the aid of the bankruptcy court Mr. Lorenzo for the second time in five years used the Bankruptcy Code to circumvent his obligations under the Railway Labor Act. Central to that statute's purpose of providing for the prompt resolution of labor disputes is each party's right to employ the "full range of whatever peaceful economic power it can muster... The Railway Labor Act depends on the assurance that neither party will be able to enlist the courts to further its own partisan end." Trans World Airlines v. Flight Attendants, 109 S.Ct. 1225, 1234, 1235. Lorenzo's reliance upon the bankruptcy court was obviously designed to thwart this legislative goal and to deprive the IAM of its right to carry on an effective strike.

Moreover, Mr. Lorenzo has again used the bankruptcy laws to discriminate between striking and non-striking employees. In a measure worthy of only the most cruel head of a major airline, Mr. Lorenzo declared bankruptcy on payday and withheld the wages that the employees had earned before the strike in an effort to increase the suffering of those who exercised their right to strike. Mr. Lorenzo, with the blessing of the bankruptcy court then paid the pre-strike wages to only those employees who have crossed the picket line.

The extent to which Mr. Lorenzo has been allowed to manipulate the bankruptcy system is reflected in how he managed to file his petition in New York when Eastern is headquartered in Miami, Florida. In anticipation of Eastern's bankruptcy Mr. Lorenzo incorporated a small subsidiary, the Ionosphere Clubs, in New York. On March 9 he filed a bankruptcy petition for this company and six minutes later filed Eastern's petition as a related case. He thus piggy-backed Eastern, a company that is two thousand times larger than the Ionosphere Clubs, into a forum that is widely accepted as a debtor's haven.

Unfortunately, this jurisdiction's reputation for favoring the debtor has proven all too true. Judge Burton R. Lifland, the judge assigned to this case, has consistently seen fit to ignore the interests of all parties except those of Frank Lorenzo and Eastern Airlines. He has regularly minimized the concerns of the employees and their representatives as "parochial interests", as if the workers that have labored for this company for so many years have less dignity than the corporate interests and should be pushed aside and ignored. Although he has proclaimed that he is motivated by the public interest in seeing Eastern return to the skies as a viable, competitive airline, these pronouncements are usually delivered in a courtroom filled with reporters and have proven to be nothing but thinly veiled partiality for Eastern Airlines. Judge Lifland has apparently embraced the view that what's good for Frank Lorenzo is good for this nation. I submit that the bankruptcy court and the examiner have been seduced by the dark side of the force.

Within the first week of the bankruptcy filing, the IAM joined with the Air Line Pilots Association and petitioned the court for the appointment of a trustee that would replace Eastern's present management. In an effort to soften the blow, Eastern responded by filing a motion for the appointment of an examiner that would investigate Eastern's corporate practices but would leave management in the control of Eastern. Judge Lifland agreed with Eastern and appointed an examiner, David I. Shapiro. Mr. Shapiro had been one of several candidates recommended to the court by Eastern Airlines. In addition to investigating the prepetition financial transactions between Eastern and its related companies -- Jet Capital, Texas Air Corporation and Continental -- the court also ordered Mr. Shapiro to assist in achieving a consensual plan of reorganization.

At the same time that Mr. Shapiro was appointed Examiner, the former commissioner of baseball, Peter Ueberroth, surfaced as a potential buyer of Eastern Airlines. On April 6 Mr. Lorenzo announced that he had reached an agreement with Mr. Ueberroth to purchase the airline that was subject, however, to the following deadline: by April 11 Mr. Ueberroth had to have successfully negotiated labor contracts with each of the three unions, the IAM, ALPA and the Transport Workers Union. From the commencement of these negotiations the unions had expressed deep concern that the structure of the Lorenzo/Ueberroth deal would require employees to return to work prior to consummation of the transaction. This meant that Mr. Lorenzo would be free to renounce the deal and thus the employees would have broken their own strike. Mr. Shapiro guaranteed us that "Lorenzo was history" and that the bankruptcy court would appoint a trustee. In this way the examiner assured the unions that the Ueberroth deal could not be abrogated and used as a strike breaking weapon by Mr. Lorenzo. Following round the clock negotiations, historic agreements were reached early Monday morning, April 10, that would have provided the new owner with $1.25 billion in concessions over the next five years. Labor proved it would make concessions to a management team it could trust.

The Examiner further advised us that he had selected Frank Carlucci, the former Secretary of Defense to serve as the trustee. We were led to believe that the selection was made in consultation with the court. Indeed, on Monday morning all the parties including Mr. Carlucci, traveled to New York and awaited Judge Lifland's approval of the Ueberroth purchase and the appointment of the trustee. However, it quickly became apparent that over the weekend the court was faced with a firestorm of opposition from

Mr. Lorenzo's counsel that he could not resist. The judge after seeking but failing to get Mr. Lorenzo's consent, sent Mr. Carlucci home. Thus, Mr. Lorenzo again prevailed over the interests of the public, the creditors and the employees.

After the demise of the Ueberroth plan the examiner with a great deal of fanfare initiated an investigation into fraudulent conveyances of assets and suspiciously low or no interest loans from Eastern to Texas Air and Continental. Prior to Eastern's filing for bankruptcy, the unions argued that Mr. Lorenzo was orchestrating a plan to strip Eastern of its most valuable assets and to upstream them either to Texas Air or Continental for a fraction of their value. One example cited by the labor organizations which, Mr. Shapiro was ordered to examine, was the sale of Eastern's computer reservations system to Texas Air for an unsecured $100 million, 6% note due in the year 2012. A major accounting firm subsequently estimated the fair market value of that note at only $35 million. Eastern's own investment banker had valued the reservations system at $250 million just one year before, and various outside financial analysts had placed its value as high as $500 million. This was only one of a series of fraudulent transactions that cry out to anyone who would perform the most cursory examination of these transactions.

In his initial report to the court, Mr. Shapiro determined that only a full scale investigation including the production of documents and the presentation of witnesses could answer all of the issues raised by these pre-petition transactions. Nonetheless upon an initial review of the most basic facts, Mr. Shapiro was able to conclude that Texas Air's and Jet Capital's control over Continental and Eastern:

> has given rise to a web of personal and financial interrelationships among the four corporations and their management that creates substantial conflicts of interest in this case. For example, Eastern's rebirth as an independent competitor to Continental might disadvantage Continental but nevertheless be in the best interest of the estate; and decisions concerning how a downsized Eastern should be configured might conflict with Continental's business interests.

Summary of Examiner's Recommendations at 2.

However, that investigation has now been stalled at Eastern's behest. The likelihood is that the examiner having embraced the Lorenzo plan will make no findings until after Eastern's plan of reorganization is approved. Thus, his ultimate findings will wittingly or unwittingly be rendered meaningless.

Following the issuance of his interim report, Mr. Shapiro took on the responsibility of assessing whether any other bona fide offers existed to purchase Eastern Airlines. Mr. Lorenzo, by that time, had already declared that Eastern was not for sale and had adopted a business plan that would substantially shrink Eastern's operations which we believe is no more than a step in the liquidation of the carrier. Mr. Lorenzo's downsizing plan requires the sale of over $1.8 billion in assets and a 40% reduction in the number of employees. Indeed, Mr. Lorenzo's strategy is nothing more than a poorly disguised liquidation, one which is cleverly designed to permit Judge Lifland and Mr. Shapiro to maintain the pretense that they are "getting Eastern back into the air" while at the same time enticing creditors with about $2 billion dollars in proceeds from these asset dispositions. Liquidation of the balance of the airline is not far behind. Our financial experts have confirmed this view. Moreover, with all due respect, we challenge this committee to call before it the legal and financial experts to the creditors committee to see if they are of a different view.

Notwithstanding his findings of substantial conflicts of interest and the bleak prospects presented by the Eastern business plan, Mr. Shapiro decided to judge the viability of any offer to purchase the airline upon whether it satisfied Eastern's only equity holder, Frank Lorenzo. "Satisfactory to Mr. Lorenzo" came to mean that he would have to receive at least $200 million in cash for a company that he only paid $275 million, then took out billions of dollars of assets and had forced Eastern to take on $700 million in new debt. Moreover, Mr. Shapiro then demanded that any potential purchaser pay as much for Eastern as Mr. Lorenzo's designated buyer had agreed to, even though Eastern was clearly losing value every day (we estimate that Eastern is now worth about $300 million less now than whatever it was worth when the Ueberroth deal was signed). He required that any potential purchaser be willing to risk $100 million more of its own money even though the Ueberroth deal did not involve one cent of risk capital. He further insisted that the purchaser accept an airline that was significantly smaller than the one Ueberroth would have bought. He argued vehemently that 22,000 employees was too many and that the number of workers that should retain employment was only 17,000. Instead of examining a business plan that would return 22,000 employees to employment, he demanded that any business plan be based on more than 17,000 employees. In sum, Mr. Shapiro's demands were mutually incompatible. At first we thought he was merely playing to the press, but, to our deep regret, we learned that his new mission is to serve the interests of Frank Lorenzo to the point that he is making every effort to break the strike. I feel both professionally and personally that the working men and women of Eastern have been betrayed.

The financial prerequisites that a potential purchaser must satisfy have been pulled out of ever changing hats by the examiner. The examiner seems to have purposely presented new and insurmountable hurdles to any potential buyers. One prospective purchaser, however, Joseph Ritchie, persevered and eventually presented a business plan that would provide Mr. Lorenzo with $200 million in preferred stock and Texas Air intra-company debt forgiveness of $259 million. The Ritchie proposal would have infused $100 million of new capital into Eastern immediately. Moreover, it would have established a safety net of $170 million in the form of additional wage concessions that would be instituted in the event Eastern suffered unexpected losses. Finally, Eastern under the Ritchie plan would resume operations with 22,000 employees but would, within several years, reach the levels of employment that existed before the bankruptcy. This plan had the full support of Eastern's three unions who are willing to make great sacrifices to insure the viability of Eastern Airlines.

The Creditors Committee was intrigued by the Ritchie proposal but concluded that unless Mr. Lorenzo consented to sell the airline it could not be a feasible offer. Mr. Lorenzo thus remained the only obstacle to a plan that would have resulted in the immediate restoration of Eastern Airlines. Although Mr. Shapiro had found that Eastern was infected with substantial conflicts of interest and although Mr. Lorenzo had himself created these conflicts, the examiner concluded that Mr. Lorenzo would control the future of Eastern Airlines. Mr. Shapiro rejected the Ritchie proposal largely because it did not satisfy Mr. Lorenzo.

Since Mr. Shapiro's announcement to the Court blindsiding the Ritchie proposal, he and Judge Lifland have embarked on a crusade on behalf of Mr. Lorenzo and his business plan. Mr. Shapiro has on numerous occasions stated: "I believe in Lorenzo's plan more than Lorenzo does." Reflexively, Mr. Shapiro has supported and Judge Lifland has approved every request by Eastern to sell assets. From the Shuttle, to numerous aircraft, to gates and slots at various airports, the court prior to approving any plan of reorganization sanctioned Mr. Lorenzo's jettisoning of these valuable and irreplaceable assets. The velocity of this process is moving like the panzer divisions over Poland. However, the court has yet to be presented with a formal Plan of Reorganization as required by the Bankruptcy Code. Moreover, Eastern has apparently convinced Mr. Shapiro to stall his investigation of the pre-petition financial transactions. Indeed, he has neither taken nor scheduled a single deposition or called a single witness.

Mr. Lorenzo desperately needs to break our strike to achieve his goal of a flying drastically reduced airline while he liquidates. Once again the court and the examiner are assisting Mr. Lorenzo in accomplishing this goal. Upon the urging of Mr. Shapiro, the court has ordered the pilots into around the clock negotiations with Eastern in a transparent attempt to force the pilots to cross the IAM picket lines. We are frankly sickened by the fact that we no longer can obtain a fair hearing from the examiner or from the court.

However, the impact of Eastern's liquidation harms the travelling public as well. The impact of Eastern's creeping liquidation has already been seen in the fares charged by other carriers. The elimination of Eastern as an effective competitor has had a tremendous ripple effect throughout the East Coast where its operations were concentrated. According to a May 9, 1989 article in the New York Times, the virtual shutdown of Eastern has permitted its competitors to use "a pricing technique known as yield management to reduce the number of discount fares available on routes served by Eastern, thus raising the effective overall price of the seats." The New York Times quotes Lee Howard, executive vice president of Airline Economics, as saying that this "is an ideal situation for yield management systems to take advantage of the shortage of seats." Yield management is little more than raising fares on routes where you enjoy a competitive advantage and the travelling public has no choice but to pay more.

There has also been a drastic decrease in the number of discounted fares in the Northeast which will not change even if Eastern's so called business plan is achieved. This plan provides that except for certain flights to Atlanta and Florida, Eastern will be virtually eliminated as a competitive presence in the Northeast. In addition, its Miami hub will be virtually eliminated due in part to the projected sale of its Latin America routes.

Most importantly, even if Lorenzo intended to fully implement his announced plan and not to either liquidate Eastern or merge it into Continental, this airline can not survive under the present circumstances. First, as more fully described by Captain Duffy, Eastern can not recruit or successfully train a sufficient number of pilots to fly either its July or August schedule. Second, the vice president of engineering and maintenance of the Air Transport Association, Clyde Richard Kizer, recently testified before this committee regarding the airline industry's critical shortage of mechanics. Based upon data collected from 14 major airlines, Mr. Kizer concluded that these carriers "have been unsuccessful in hiring mechanics at the rate needed. In total these airlines are short more than 4000 mechanics to their current needs. These are hiring needs that have been approved and funded, but for which there are inadequate numbers of qualified candidates." According to Mr. Kizer, "approximately 2-3 years of formal and on the job training is required to achieve full productivity from a recently schooled mechanic."

We have attempted, to the best of our ability, to closely monitor Eastern's maintenance situation -- especially as it attempts to put more planes in the air over the next several months. What we have learned, from what I believe to be very reliable sources, is that Eastern's maintenance program is in utter shambles. Eastern is woefully understaffed in virtually every maintenance area, and the "mechanics" they do have are predominantly either unskilled mechanics "helpers" or people who are right out of training school. Here are some examples of Eastern's maintenance crisis:

While Eastern's July schedule calls for the equivalent of about 65 aircraft, they plan to utilize 107 in order to postpone required maintenance as much as possible. If it actually attempts to fly its August schedule, which calls for the equivalent of 95 aircraft, they will almost certainly run out of spare aircraft that are operationally fit to fly.

Right now, Eastern has over 30 aircraft that are "out of time," and are simply sitting on the ground waiting for required maintenance checks. Eastern has already used up all of its spare engines and has been forced to pull another 30 off the wing.

In order to meet the maintenance requirements of their plan, Eastern needs to overhaul 5 engines per week in August. We believe that they will be lucky to get 5 per month out of that severely understaffed and inexperienced shop. We believe that they currently have about 100 very inexperienced mechanics in the engine shop. However, just prior to the strike, there were about 600 mechanics producing 20-to-22 engines per month.

In addition, we have learned that Eastern has only about ten people working in the wheel and brake shop while they need at least 4 times that number to service the requirements of their planned August operation. They will require at least 500 wheels and brakes during that month. Eastern also has a critical shortage of sheetmetal mechanics. Indeed, Eastern probably has fewer than 50 systemwide. These mechanics are required to "unbutton" aircraft before the rest of the needed mechanical work can be performed, and then they have to button the aircraft back up again. Normally, a "C" check line, for instance, is staffed with 55% sheetmetal mechanics and 45% A & P mechanics.

Eastern has scheduled its "C" check line in Atlanta to perform one "C" check ever 2-1/2 days. Even with experienced mechanics, the 2,500 man hours per aircraft they have scheduled for each aircraft would normally take 4-to-6 days. Since they have shifted their supervisors over to line maintenance in an attempt to cover their requirements there. Eastern has nothing but "green" mechanics on their "C" check line. They will be lucky to get one airplane out every 6-to-10 days with that crew.

Since the strike, Eastern has accumulated tens of thousands of man hours in backlog for repair of parts. It has been borrowing parts from wherever they could find them.

Ironically, Eastern's rush to sell assets has itself placed a major strain on its ability to maintain its scheduled level of operations. Many of the aircraft it has sold, or plans to sell, require minor to intensive maintenance prior to delivery. They have been forced to dedicate their "D" check lines in Miami solely to these requirements, and they are falling far behind schedule. For example, Eastern's own maintenance schedule says that the last of the Trump 727s will be completed by the end of July. In fact, it is now clear that this will not be completed until September. Eastern is selling 15 aircraft to UAS, and each of those aircraft require some work (some minor, some extensive). This is all supposed to be completed by July 17. However, there is no way that Eastern will meet that deadline. It will probably slip by a month or more. Also, Eastern's heavy maintenance schedule reflects that it is planning to sell 11 additional aircraft to Continental. Of those aircraft, 5 require "D" checks, with a schedule of 31,000 man hours per aircraft (which is extremely optimistic given the inexperience of their mechanic workforce). Eastern is planning on doing at least three of those checks in-house, plus varying degrees of work on the rest. Simply to attempt to meet its commitments with respect to the aircraft it is selling, Eastern will be forced to dramatically undermine its operational maintenance capabilities.

In the avionics area, they are also in deep trouble. They have no one other than supervisors trying to work the incredible parts backlog in that shop. They have already used every piece of avionics equipment they could find in the system.

The simple fact is that Eastern's schedule will not operate in August with the mechanical workforce they currently have. The severity of Eastern's maintenance problems are demonstrated by its reliance upon secretaries, reservations clerks and sales managers to perform critical maintenance work. For example, totally inexperienced white collar workers were used to do an annual "C" check on a DC-10. A "C" check is a heavy maintenance inspection that involves almost the entire rebuilding of the aircraft. These three and half dozen on-the-job trainees did everything from building landing gear and brakes, taking apart engines, checking complicated electronic circuitry to inspecting the airframe. What makes matters worse is that their work was supervised by managers, who, themselves, haven't physically performed such work for possibly ten to twenty years.

A newspaper report included quotes from these workers in which they proclaimed their newly discovered ability to repair aircraft. For example, an attorney stated "After 30 years as an aviation lawyer, I'm finally getting my hands on the greasy parts..." A sales manager confided "I didn't even know how to use a ratchet or a screwdriver three weeks ago." Obviously our safety concerns predated the strike. However, these developments have caused us to sound the alarm and pray that it will be heard.

Finally, even when Eastern's management has had qualified mechanics to perform the work, as it did prior to the strike, it resorted to falsifying maintenance documents. An FAA investigation at Kennedy Airport recently revealed that supervisors regularly signed work sheets falsely indicating that essential maintenance had in fact been performed. As a result of this investigation Eastern Airlines last month surrendered its repair station certificate. On June 23, 1989, the FAA issued another report in which it determined that Eastern's maintenance systems at Miami and Atlanta failed to make needed repairs to malfunctioning aircraft even after receiving repeated complaints from pilots. The documents upon which the FAA based this conclusion include records of airplanes repaired after the strike commenced which are dated as recently as May 29, 1989. The FAA has initiated another investigation into maintenance practices at LaGuardia Airport which was again prompted by reports of management requiring foremen to falsify documents.

The implementation of Eastern's purported business plan is thus severely, if not fatally, undermined by its failure to employ a sufficient number of qualified mechanics and pilots. Furthermore, Eastern's management is incapable of safely operating whatever additional flights it initiates. Mr. Lorenzo's ongoing liquidation of the airline while its staffing and safety standards deteriorate guarantee the demise and ultimate disappearance of Eastern Airlines.

Another critical motivating force behind Mr. Lorenzo's sham business plan is his desire to escape from Eastern's $750 million in unfunded pension liabilities. The Employee Retirement Income Security Act ("ERISA") provides that Eastern's affiliated companies including Texas Air may be obligated to assume these liabilities in the event Eastern's pension plans are terminated or the airline is liquidated. By maintaining the facade of Eastern as a functioning carrier Mr. Lorenzo hopes to dissuade the Pension Benefit Guaranty Corporation ("PBGC") from demanding that Texas Air Corporation or Continental fulfill these funding obligations. In early April the PBGC expressed its concern that if Eastern sold the Shuttle it would no longer be a viable airline. In fact, three weeks after the Shuttle was sold Eastern found it necessary to request that the IRS waive the $100 million pension contribution which is due in September. Nevertheless, the PBGC has taken no action whatsoever to ensure that the benefits of thousands of retirees and the future of the PBGC itself be put at risk. Obviously, as long as Lorenzo continues to perpetuate the myth that liquidation is not the ultimate consequence of his business plan, the PBGC will do nothing. It will not invoke those provisions of ERISA which are specifically designed to protect against a situation such as this. Those employees who dedicated their working lives to Eastern Airlines should not have their retirement years jeopardized by corporate greed and bureaucratic inaction.

Conclusion

Mr. Chairman, since Frank Lorenzo took over Eastern Airlines in late 1986, has systematically looted this once-proud carrier -- for the benefit of Texas Air and its other airlines subsidiary, Continental. The record is replete with evidence that Eastern has been used as a spare-parts airline for non-union Continental.

In spite of his amply documented destruction of Eastern as a major competitive force in the airline industry, Mr. Lorenzo is receiving significant assistance from the judiciary and the executive branch in furtherance of his ultimate goal: The complete liquidation of Eastern.

The White House and the Secretary of Transportation actively encouraged the labor-management confrontation that was immediately followed by Eastern's bankruptcy filing. Judge Lifland is knowingly permitting Mr. Lorenzo to implement his plan even prior to formally submitting it for confirmation. The Examiner, whom we are confident is acting on written orders of Judge Lifland, is moving heaven and earth in an effort to break our strike.

While the Administration and Judge Lifland have given lip service to the same policy goal: To further competition in the airline industry. Unfortunately, the Administration's actions have led to the precise opposite result, as Eastern disappears as a viable, national competitor. Even if Mr. Lorenzo's stated pla were fully implemented, there will indisputably be much les competition in the future. Months after the Administration' position blew up in its face, it is still maintaining an ostrich like posture -- hoping no one will notice the abject failure of it policy. Even at this late hour, the Administration has taken n step whatsoever to rectify the severe damage it has inflicted o airline competition.

While Judge Lifland has repeatedly said he wants to se Eastern "get back up in the air," he has retreated to th traditional bankruptcy court priorities-protection of the debto and accommodation of the creditors and let the employees be damned Neither the debtor, nor its sole stockholder, Texas Air, nor th creditors have any inherent interest in fostering competition i the airline industry. In fact, their interests are only to tea as much from Eastern's carcass as possible.

Thus, we have a public policy dilemma of major proportions The executive branch has the authority and the obligation to foste airline competition, but it has been deeply embarrassed and lack the inclination and the courage to intervene to protect the publi interest. The judiciary -- in the form of Judge Lifland -- on th other hand, is responding to interests that do not in any wa encompass the public interest in effective airline competition o stable labor relations.

Time and again, the Congress has taken strong steps to foste competition in the airline industry. It is clear that, in the case of Eastern Airlines, congressional intent is being deeply undermined.

Mr. Chairman, it is time once again for Congress to act. Only you can reverse the competitive disaster that is looming. We stand prepared to assist you and your staff in devising the solution to this crisis.

Mr. OBERSTAR. Thank you for being here so long. Our next witness is Mr. Henry Duffy, President of the Air Line Pilots Association. Mr. Duffy, welcome to the evening portion of this hearing and would you please identify your associates for the record.

TESTIMONY OF HENRY A. DUFFY, PRESIDENT, AIR LINE PILOTS ASSOCIATION, ACCOMPANIED BY CAPTAIN JACK BAVIS, CHAIRMAN, EASTERN MASTER EXECUTIVE COUNCIL; FARRELL KUPERSMITH, ASSOCIATE MANAGING PARTNER, TOUCHE ROSS AND CO.; AND BRUCE SIMON, OFFICE OF GENERAL COUNSEL

Mr. DUFFY. Mr. Chairman, on my left is Captain Jack Bavis, who is Chairman of the Eastern Master Executive Council. He heads the Eastern pilots. On my far right is Mr. Farrell Kupersmith, who is the Associate Managing Partner of Touche Ross and Company and our financial advisor. And to my immediate right is Mr. Bruce Simon, Office of General Counsel.

Mr. Chairman, given the late hour, I am going to be short in my statement. I hope you will understand that that in no way takes away from the anger and deep emotion, I think, that you heard in John Peterpaul's voice and certainly you will hear in mine and Mary Jane Barry's, who probably follows us in the next panel about what we see as destruction of this great airline.

As you well know, five and a half years ago, Continental Airlines filed for protection under the bankruptcy laws. The carrier unilaterally abrogated all of its contracts with its represented employees and slashed those employees' wages nearly in half. It undertook a reorganization plan that provided full payment for all of its creditors, except employees. It then refused to deal further with its unions, the IAM and ALPA.

Now the owner of Continental, Mr. Frank Lorenzo, has placed another major airline into bankruptcy and once again he seems bent on breaking his contracts with his labor unions. But because it is unlikely that he will successfully reorganize Eastern, it appears at this time the big losers will not only be Eastern's employees, but the traveling public as well. Accordingly, I am here today to urge you to take action to stop what I believe is a calculated abuse of the bankruptcy process and a systematic liquidation of a once premier airline that undermines the public interest.

Shortly after Mr. Lorenzo gained control of Eastern he began to strip its assets for the benefit of Texas Air Corporation and its other subsidiaries, especially nonunion Continental. The transfers took many forms: the sale of Eastern's assets and services for less than they were worth, the forced purchase by Eastern of assets and services from Texas Air and its subsidiaries for more than they were worth, the operation of Eastern to enhance the interests of Texas Air and its other subsidiaries, and the lending of cash to affiliated companies.

These transactions and several others are explained by Mr. Kupersmith in a filing for the bankruptcy court and we have entered them into the record. I will not go through them now, but you know about them all—the CRS transfer and the fuel tax that Continental management imposed on Eastern.

Mr. **Oberstar**. In short, Mr. Lorenzo has gotten out of Eastern already more than he put into it originally.

Mr. **Duffy**. It has been a constant, steady, never-ending flow of assets and cash towards Continental and towards Texas Air and up the line. From its inception the downsizing and asset stripping scheme has undermined Eastern's financial condition. After four consecutive quarters of profitability largely fueled by employee concessions, the carrier began to lose money in the third quarter of 1987, and as the downsizing continued through that year in 1988, the losses accelerated.

Not surprisingly, Eastern has maneuvered itself into the bankruptcy court. Mr. Chairman, this is Mr. Lorenzo's briar patch. Here there is a happy tangle of laws and regulations favorable to a debtor where Mr. Lorenzo can unleash his considerable army of lawyers and advisors to escape his legal obligations and to frustrate the operation of the labor laws, the transportation laws and the public interest. Here, an automatic stay of all litigation against the debtor insulates Mr. Lorenzo from the myriad of pending court cases brought by his own shareholders, his creditors, and the employees.

The same stay prevents employees from processing grievances to obtain contractual rights unilaterally withheld by the company. Bankruptcy is where Mr. Lorenzo knows he can attack his labor agreement without having to comply with the rules of the Railway Labor Act, as do all of his other competitors. And here he can continue apace with the liquidation of Eastern.

To be sure, Eastern has submitted a business plan which outlines how it plans to fly its way out of bankruptcy and to pay its creditors. But a bird cannot fly when its wings are clipped and surely Mr. Lorenzo has clipped Eastern's wings. Following in the wake of the sale of Eastern's last profitable component, the Eastern Shuttle, and the relinquishment of numerous routes and airplanes, the plan holds little prospect of success. It is based upon unrealistic assumptions with respect to fleet utilization, revenues, and as we know too well, pilot recruitment training and productivity.

In any event, based on its recent performance of treating Eastern as a cash cow for the rest of Texas Air, is anybody to believe that Texas Air management is really interested in creating a viable Eastern? Are they really playing out the last chapter of a very cynical game in which Eastern, its employees, and the public are the big losers? Unless Eastern is sold to Mr. Ritchie or someone else with the desire and the ability to restore it to a competitive state, what do we all have to look forward to?

Certainly there will be the loss of thousands of good, fair paying jobs with the consequent widespread disruption to personal and community lives. There will also be the loss of yet another major carrier in an industry that has seen the loss of nearly half its major companies in the last three years. Both personal experience and recent studies demonstrate that this diminution in competition is showing up in the form of marked fare increases, particularly at hubs dominated by a single carrier. In this regard, Congress should be aware, and I know you are, Mr. Chairman, that Mr. Lorenzo's other carrier, Continental, is also on the endangered carrier list. They lost $315 million last year. They have got company imposed

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lowest major carrier labor cost in the industry, and they still cannot make money.

And finally, there may well be an actual financial liability on the part of the entities outside of Texas Air. The Pension Benefit Guarantee Corporation which guarantees that certain pension plan obligations are paid may be required to cover some or all of Eastern's unfunded pension liabilities. These are estimated by the PBGC at approximately $700 million without even counting the massive health and welfare obligations for Eastern's retirees, and as merely a contingent creditor in Eastern's bankruptcy, the PBGC will not participate in any distribution under any Eastern reorganization plan.

Before closing and taking questions, I would like to address one aspect of the predicament of how Eastern got to where it is and that is the actions of the Government agency tasked with monitoring Eastern's continuing fitness, the Department of Transportation.

Last spring DOT headed off a Congressional effort to mandate a fitness review of Eastern by conducting a preliminary investigation of Eastern. But the Department expressly refused to analyze the impact of the transfer of Eastern's assets to Texas Air and its subsidiaries on the grounds that the transfers were of no concern as long as, and I will quote, "Texas Air has the commitment and the resources" to cover Eastern's shortfalls. By this refusal DOT ignored the findings of the Defense Contract Audit Agency which it hired to assist with the preliminary investigation. Those findings were that many of the intra-Texas Air transactions that they examined appeared to be detrimental to Eastern. Moreover, the Department failed to explore Texas Air's alleged commitment to provide resources to Eastern.

Several months later, DOT rejected a petition by ALPA to initiate a fitness review of Eastern. In that rejection Secretary Burnley made clear that the economic condition of Eastern was of no concern to DOT as long as the safety of Eastern was not compromised. Astoundingly, shortly after he issued that decision, Mr. Burnley went to work for a law firm for the express purpose of representing Eastern and Continental in transportation matters.

In sum, Mr. Lorenzo, no matter what he says, is not an airline builder. You cannot build a successful airline by feeding your employees a daily gruel of lies, threats and distortions. Indeed, in the long run, you cannot build anything worthwhile on a structure of fractured promises and broken commitments. Congress cannot make Frank Lorenzo an enlightened employer, but it can take action to prevent him from looting Eastern to suit his own private interests. Mr. Chairman, Congress should take those actions immediately. Thank you.

Mr. OBERSTAR. Thank you very much, Captain Duffy. I wish the Senate had acted back in March when we passed our legislation. I think the world of Eastern would be much different today. The lot that your colleagues and pilot corps would be much different than it is today, and the world of competition in the airline industry would be much healthier than it is or is likely to be for some time to come.

A question that I have is that Mr. Bakes said that pre-strike, according to the notes I made, the average flight time of the pilots they hired was 4,300 hours, post-strike, 5,700 hours experience, and that they are training these pilots to Eastern standards, and, in fact, that the new pilots are going to be receiving more training than pilots at other airlines. And that they are going to meet their targets for the numbers which are still in some dispute for August. Are you satisfied that, first of all, that the pairing issue of experienced and inexperienced pilots working together is going to be adequately addressed? That the training program is satisfactory? Finally, that those numbers of hours of experience prior to hiring are reliable?

Mr. DUFFY. Mr. Chairman, that whole forecast looks like a piece of swiss cheese. It has got so many flaws in it, I do not know where to begin. Let me say that first of all, the utilization that is forecast for pilots simply does not exist anywhere in the industry and we do not think it can be met under any circumstances. They are not going to be able to get the number of hours out of the number of pilots that they forecast, that they put out there on the line. But more fatal than that is the fact that they are not going to be able to graduate the number of pilots that they say they can.

We think there are about 30 percent, but whatever that number, what is starting to happen in the Eastern system is the inexperience of the new hire entry that is coming in over there. I do not doubt Mr. Bakes. They are going to give them more school because they are going to need it. They have gone out and raked their way through all the fixed base operations. They have got a bunch of general aviation pilots. Nothing against general aviation pilots, but it is simply not up to the quality of new entry that we have been accustomed to seeing in this industry.

And they play these average games. They will give you an average of an age or an average of the number of hours, but what they have done is brought some retired militaries in who are older and have a lot of hours and paired them with some much younger and much more inexperienced pilots and created some averages. That is not what we are concerned with. It is not the averages. What is the median? What is the experience of those pilots coming in?

And then to get to your point, the pairing question. I got here kind of at the end of Mr. Bakes statement, but I did hear him say this marvelous thing that they were going to do about high minimums. Well, I hate to tell you what adding minimums to a predominate group of pilots operating in the winter into Atlanta in competition with other airlines flying Category 3A minimums in the fog or when the sea fog comes rolling into Kennedy, having airplanes that are going to be going somewhere else because all the pilots are on high minimums. It is going to be devastating to the operating plan that we think already had many shortfalls.

When the Continental accident at Denver took place, ALPA was very hesitant to sign on to the pairing question because the airlines had operated for many years without really giving that a lot of consideration, but I want to emphasize that our hesitance was in a normal airline situation where in a chance situation two inexperienced pilots being paired together is pretty remote, not with this huge group of new fledgling pilots being pushed out into the airline environment.

And I think it is a dangerous situation, Mr. Chairman, and it is something that the FAA is going to need to stay right on top of because we have very great concerns.

Mr. OBERSTAR. Are FAA personnel watching this training program close enough in your judgment?

Mr. DUFFY. I guess they will never watch it carefully enough for us, Mr. Chairman. The problem to a certain extent has not evidenced itself because we are in the initial stages of starting to crank these people through the schools, and certainly we have not seen enough new people out in the line for this pairing problem to start to add it into itself just beginning now. Unfortunately, it will evidence itself right when the bad weather comes in as we move into the winter operation, and that is the last place you want to experience a problem like that.

Mr. OBERSTAR. Thank you. Is ALPA a member of the Creditor's Committee?

Mr. DUFFY. Yes, we are.

Mr. OBERSTAR. As a member of that committee, have you seen the business plans submitted by Eastern?

Mr. DUFFY. Let me ask Mr. Simon.

Mr. OBERSTAR. Do you know whether any of the other creditors or their advisors have seen and have been able to review and react to Eastern's business plan?

Mr. SIMON. The creditors received a flip chart presentation with single bullet points on it and some pages left deliberately blank. Some portions of it we were excluded, most specifically the portions that dealt with pilot training and pilot availability and the issues we have just been addressing. We were told that the Committee's professionals have seen backup data. We are unfortunately under a confidentiality cloaks, something that it occurs to me that separation of powers notwithstanding the Committee, you may want to focus on a little bit. Not simply the confidentiality that we are under the Creditor's Committee, but the black hole into which the examiner's entire investigation and pre-petition obligations has gone.

In that connection, some observations were made by the Committee's professionals regarding the viability of the Lorenzo plan that were not consistent with what was reported to you today by the examiner. But because we are under a confidentiality cloak, I do not quite know how to respond to that unless directed by the Committee.

Mr. OBERSTAR. Are you able to comment or make comparisons between the new business plan and the plan submitted by Mr. Ritchie?

Mr. SIMON. We have also obviously been made knowledgeable of the Ritchie plan, yes. I think Mr. Kupersmith would probably be a better person to comment on the relative financial viability consequences of the two plans. He too was to some extent burdened by the cloak of confidentiality with respect to the Lorenzo plan.

Mr. OBERSTAR. Gagged in other words?

Mr. SIMON. That is to put it mildly. We are reminded with great regularity about the imposition of that secrecy portion.

Mr. OBERSTAR. Something that I found very puzzling in the testimony of Mr. Shapiro. The bankruptcy judge is proceeding on the basis of consensual agreement and not using wars, and there may not be any tools for court directed action, coercive action. But kept insisting that if there was not a consensual solution to an outside purchase, then litigation over an outside purchase could go on for years, and the company would lose its assets. Is it possible to achieve a non-consensual solution within the confines and the constraints or limitations of the bankruptcy law?

Mr. SIMON. Absolutely.

Mr. OBERSTAR. Could you explain to us on how that could be achieved?

Mr. SIMON. Well, one place to look is in other instances. For example, in Sharon Steel, one of the Nation's largest steel companies, formerly under the direction and control of another person with some degree of notoriety and American industrial annals, Victor Posner. Mr. Posner put the company into bankruptcy. Many of the same kinds of allegations, of conflict of interest, of asset stripping, of cannibalization of the company were made in that case, as are made in this case.

The bankruptcy court judge in that case imposed a trusteeship. The trusteeship took effect the day it was imposed. There has been litigation with regard to that matter subsequently. Then recently, the Third Circuit Court of Appeals approved the appointment of a trustee. The fact of the matter is that dependency of litigation made no difference whatsoever. The case was instantly taken out of the hands of the person found by the bankruptcy court to have raped the company. The person charged had his due process course of appeals, but the company was put into the independent hands of someone who ran the company in the interest of the constituents of the company while litigation played itself out.

There has been some talk here today about the fact that the Bankruptcy Code, as you described it, is a blunt instrument or may not be adequate to the task. And I think in many respects that is the case. But that is not the end of the situation. There are tools available under the Bankruptcy Code that could be applied in this instance and simply have not been.

Mr. OBERSTAR. Is that because the judge is unwilling to operate that way or because Mr. Lorenzo has objected through his lawyers to any such actions?

Mr. SIMON. The first, the latter, then the former. The fact of the matter is as the examiner testified today, he was the one that recommended the appointment of the trustee. This canard that it was insisted upon by the unions should once and for all be put to rest by the examiner's own testimony today. The trusteeship was not forwarded by or demanded by or insisted upon by the unions. The trusteeship was the examiner's construct. It was recommended to the employee groups as the price for extracting the concessions from the employee's hides to the tune of over a billion dollars. The unions acquiesced. The examiner, Mr. Shapiro, went to the court and presented to him the request for the trustee. That request, I may add, was supported by the United States trustee, an agent and a part of the United States Department of Justice.

Mr. OBERSTAR. What did the judge do?

Mr. SIMON. He did not appoint a trustee.

Mr. OBERSTAR. Why?

Mr. **Simon**: I wish he were here in this chair to answer that question.

Mr. **Oberstar**. He issued no finding, no explanation, just refused to do it?

Mr. **Simon**. That is correct.

Mr. **Oberstar**. The examiner believes, at least that is the sum of his testimony, that Eastern cannot operate successfully unless the debt load is reduced. And that the way to reduce the debt load is to sell assets to pay off debt. A number of $1.8 million is the figure used in reducing that debt load. Does the ALPA group concur in that view? Is that the only way to reduce the debt load? Are there other ways to reduce the debt burden?

Mr. **Kupersmith**. Yes, sir. The remarks by Mr. Shapiro are really out of context for several reasons. First of all in the Ritchie proposal, there was a capital infusion of $100 million to Eastern Air Lines, and while I heard Mr. Shapiro use words like minimal to describe it, it is nevertheless $100 million more than Texas Air is putting into Eastern Air Lines.

Secondly, the employee wage concessions of greater than a billion dollars that Mr. Simon just alluded to substantially expand the operating income of the airline, such that the management of the debt load is substantially more advantageous than it is in the Lorenzo plan.

Thirdly, the concept of critical mass in the Ritchie proposal is approximately 200 airplanes, and even under the Ritchie proposal, there is still a substantial sale of assets that would occur to largely reduce the debt load. So we are talking about a relatively insignificant amount of debt between the two plans, but one plan has the benefit of a major capital infusion and substantial employee concessions, and in that context Mr. Shapiro's comment on financial feasibility we believe is incorrect, as is agreed to by Shears and Leaman, one of the biggest financial institutions in the country.

Mr. **Oberstar**. Beyond the Ritchie proposal, are there other third party interests willing to step forward and able to step forward with a credible, viable, operational and financial plan?

Mr. **Kupersmith**. There have been a number of inquiries, but fundamentally people have felt that the criteria that have been established by the court are illogical, if I can use that term. In April of this year, Texas Air agreed to sell Eastern Air Lines to Peter Ueberroth for $464 million. By their own admission and sworn testimony in court, Eastern Air Lines has lost between $3 and $4 million per day since that. And I would like to just reconcile that versus the $1.7 million. The $1.7 million is cash going out on a daily basis. The difference between the $1.7 and the $3 to $4 million is the amount of accrued interest and other liabilities that will have to be paid to emerge from bankruptcy.

So the actual economic loss is in excess of $3 million a day. By my count, more than 70 days have past with losses of greater than $3 million per day by their own sworn testimony. That is in excess of $200 million reduction of value. Mr. Shapiro said it would be aberrational if someone offered that to Mr. Lorenzo and he refused. And indeed it would because the $464 million, if it were worth that in April, obviously it is worth at least $200 million less today by their own admission of losses.

The problem with respect to other third parties who have come forward and expressed an interest is that they have viewed Mr. Shapiro's and the court's insistence that somebody pay $464 million is aberrational and consequently other third parties who have been willing to come forward have been discouraged by what they view to be insurmountable obstacles being put in their way.

Mr. **Oberstar**. Your conclusion, or I conclude from your statement, that it is not possible for Mr. Ritchie to do as the examiner proposed, that is offer the Ueberroth deal minus the walk-away provision and then thereby put Mr. Lorenzo in a position of either accepting or rejecting. If he rejects it, then not negotiating in good faith or being of bad faith negotiator. In which case then, he suggested that it would be possible for the court to exercise some leverage.

But you are suggesting that this time it is not financially sound or responsible to offer the dollar amount of the Ueberroth deal?

Mr. **Kupersmith**. Notwithstanding my previous comments, and my answer to that would be, yes. But notwithstanding my previous comments, the employees and perhaps it is a measure of how much the employees of Eastern Air Lines are committed to its resuscitation as a viable company. Have committed as part of the Ritchie proposal to underwrite $200 million of the $464 and therefore in effect the employees are swallowing the losses through additional concessions by underwriting $200 of the $464.

So, if you will, the third party financier structure is committed to $262 and the employees are really filling in the difference. It is not logical, but the employees nevertheless have committed to do that. So, if you will break the bondage and get on with coming back to work under a different management structure. So the employees in effect have bridged the gap between what people would say is feasible and logical and what the court has said could get done, if in fact, somebody comes forward with that.

Mr. **Oberstar**. One final point that I think that I should raise because it will give me an opportunity to say something on the record about it. And that is, that there is a report circulating that, Captain Duffy, that the Air Lines Pilots Association is calling on its membership to slow down and disrupt travel over the 4th of July weekend. Would you respond to that?

Mr. **Duffy**. That is not true, Mr. Chairman.

Mr. **Oberstar**. Thank you, I did not think it would be, but those reports have circulated in various quarters, and I think you ought to have an opportunity to respond to it.

Mr. **Duffy**. Thank you.

Mr. **Oberstar**. I have no further questions.

Mr. **Duffy**. Mr. Chairman, Captain Bavis had a written statement. Because of the late hour, we would like to simply submit that for the record.

Mr. **Oberstar**. That will be accepted and included in the record at this point.

Mr. **Duffy**. Thank you.

[Prepared statements of Mr. Duffy and Mr. Bavis follow:]

STATEMENT OF

HENRY A. DUFFY, PRESIDENT

AIR LINE PILOTS ASSOCIATION

BEFORE THE

SUBCOMMITTEE ON AVIATION

COMMITTEE ON PUBLIC WORKS AND TRANSPORTATION

U. S. HOUSE OF REPRESENTATIVES

JUNE 29, 1989

THE CURRENT CONDITION OF EASTERN AIRLINES AND ITS PROSPECTS FOR RESTORATION AS A MAJOR CARRIER

Good morning, I am Henry Duffy, the President of the Air Line Pilots Association (ALPA). With me are Captain John Bavis, Chairman of the Eastern pilots Master Executive Council, Bruce Simon of the law firm Cohen, Weiss & Simon which represents ALPA in the Eastern bankruptcy proceedings, and Mr. Farrell Kupersmith, the Associate Managing Partner of Touche Ross & Co., which has provided financial evaluation services to ALPA with respect to Eastern Air Lines.

Five and a half years ago Continental Airlines filed for protection under the bankruptcy laws. The carrier unilaterally abrogated all of its contracts with its represented employees and slashed those employees' wages nearly in half. It undertook a reorganization plan that provided full payment for all its creditors except employees. It then refused to deal further with its unions - ALPA and the IAM.

Now the owner of Continental, Mr. Frank Lorenzo, has placed another major airline into bankruptcy and once again he appears bent on breaking his labor contracts and his labor unions. But because it is unlikely that he will successfully reorganize Eastern, it appears that this time the big losers will not only be Eastern's employees but the travelling public as well. Accordingly, I am here today to urge you to take action to stop what I believe is a calculated abuse of the bankruptcy process and a systematic liquidation of a once premier airline that undermines the public interest.

Shortly after Mr. Lorenzo gained control of Eastern he began to strip its assets for the benefit of Texas Air Corporation and its other subsidiaries, especially non-union Continental. The transfers took many forms: the sale of Eastern's assets and services for less than they were worth, the forced purchase by Eastern of assets and services from Texas Air and its subsidiaries for more than they were worth, the operation of Eastern to enhance the interests of Texas Air and its other subsidiaries, and the lending of cash to affiliated companies.

Among the most outrageous of these transactions were:

(1) Eastern's sale of its computer reservation system (valued at several hundreds of millions of dollars) to a Texas Air subsidiary for a subordinated 6 percent note with a face value of $100 million payable in the year 2012 after which Eastern paid Texas Air $10 million a month for the privilege of using its own CRS;

(2) Eastern's payment to Texas Air subsidiary of a surcharge of 1 cent per gallon for all airplane fuel with no measurable benefit in return;

(3) Eastern's funding of Continental's purchase of Bar Harbor Airlines;

(4) Eastern's purchase of an unmarketable, 10 percent, unsecured People Express note for $25 million in cash from Texas Air, a deal that generated a $4.4 million profit for Texas Air at a time when Eastern was short of cash;

(5) Eastern's sale of gates at Newark airport to Continental for bargain prices; and

(6) The attempted transfer of the Eastern Shuttle to a Texas Air subsidiary, also at a bargain price, which luckily was derailed by a federal judge.

These transactions and several others are explained in detail in the declaration of Mr. Kupersmith which accompanied

ALPA's motion for the appointment of a trustee in the bankruptcy case and which has been submitted for the record.

From its inception, the downsizing and asset stripping scheme has undermined Eastern's financial condition. After four consecutive quarters of profitability largely fueled by employee concessions the carrier began to lose money in the third quarter of 1987 and, as the downsizing continued through that year and 1988, the losses accelerated.

Not surprisingly, Eastern has maneuvered itself into the bankruptcy court. This is Mr. Lorenzo's briar patch. Here there is a happy tangle of laws and regulations favorable to a debtor where Mr. Lorenzo can unleash his considerable army of lawyers and advisors to escape his legal obligations and to frustrate the operation of the labor laws, the transportation laws and the public interest. Here an automatic stay of all litigation against the debtor insulates Mr. Lorenzo from the myriad of pending court cases brought by his own shareholders, creditors and employees. The same stay prevents employees from processing grievances to obtain contractual rights unilaterally withheld by the company. Mr. Lorenzo has even taken the position, incorrectly, we believe, that the stay prevents the National Mediation Board from issuing a decision on whether Eastern and Continental have been operated as a single carrier for labor relations purposes. Bankruptcy is where Mr. Lorenzo knows he can break his labor agreements without having to comply with the rules of the Railway Labor Act as do all his competitors. And here he can continue apace with the liquidation of Eastern.

To be sure, Eastern has submitted a business plan which outlines how it plans to "fly" its way out of bankruptcy and to pay its creditors. But a bird can't fly if its wings are clipped and Mr. Lorenzo has seen to that. Following in the wake of the sale of Eastern's last profitable component, the Eastern Shuttle, and the relinquishment of numerous routes and airplanes, the plan holds little prospect of success. It is based upon unrealistic assumptions with respect to fleet utilization, revenues, and pilot recruitment, training and productivity. For example, Eastern projects that it will suffer no net loss in revenues after adjusting for the size of the airline. But this projection ignores the experience of Continental which suffered from markedly reduced yields after its bankruptcy and the serious operational and consumer problems that Eastern's management faces. A detailed critique of Eastern's revenue projections and other components of the business plan prepared by ALPA's economics department an ALPA analysis of Eastern's pilot training and hiring capability, and an article from Tuesday's Boston Globe questioning the quality of Eastern's new hire pilots have been submitted for the record.

In any event, based on its recent performance of treating Eastern as a cash cow for the rest of Texas Air, are we to believe that Texas Air management is really interested in creating a viable Eastern? Aren't they really playing out the last chapter of a cynical game in which Eastern, its employees and the public are the big losers? Unless Eastern is sold to Mr. Ritchie or someone else with the desire and ability to restore it to a competitive state what do we have to look forward to?

Certainly there will be the loss of thousands of good, fair paying jobs with the consequent widespread disruption to personal and community lives.

There will also be the loss of yet another major carrier in an industry that has seen the loss of nearly half its major companies in the last three years. Both personal experience and recent studies demonstrate that this diminution in competition is showing up in the form of marked fare increases, particularly at hubs dominated by a single carrier. In this regard Congress should be aware that Mr. Lorenzo's other carrier, Continental - which has management imposed wages of far below those of other carriers and thus can hardly complain of high labor costs - is in a precarious position itself. Last year that carrier lost $315.5 million, a year of record profits elsewhere in the industry, notwithstanding Mr. Lorenzo's efforts to shore it up by pillaging Eastern. This year Continental has continued to be unprofitable and has suffered continued declines in capacity and traffic.

And finally, there may well be an actual financial liability on the part of entities outside Texas Air. The Pension Benefit Guarantee Corporation which guarantees that certain pension plan obligations are paid may be required to cover some or all of Eastern's unfunded pension liabilities. These are estimated by the PBGC at approximately $700 million without even counting the massive health and welfare obligations for Eastern's retirees, and as merely a contingent creditor in Eastern's bankruptcy, the PBGC will not participate in any distribution under an Eastern reorganization plan.

Before closing and taking questions I would like to address one aspect of the predicament of how Eastern got to where it is and that is the actions of the government agency tasked with monitoring Eastern's continuing fitness -- the Department of Transportation.

Last spring DOT headed off a Congressional effort to mandate a fitness review of Eastern by conducting a "preliminary investigation" of Eastern. But the Department expressly refused to analyze the impact of the transfer of Eastern's assets to Texas Air and its subsidiaries on the grounds that the transfers were of no concern as long as "Texas Air has the commitment and the resources" to cover Eastern's shortfalls. By this refusal DOT ignored the findings of the Defense Contract Audit Agency, which it hired to assist with the preliminary investigation, that many of the intra-Texas Air transactions they examined appeared to be detrimental to Eastern. Moreover, the Department failed to explore Texas Air's alleged "commitment" to provide resources to Eastern.

Several months later, DOT rejected a petition by ALPA to initiate a fitness review of Eastern. In that rejection Secretary Burnley made clear that the economic condition of Eastern was of no concern to DOT as long as the safety of Eastern was not compromised. Astoundingly, shortly after he issued this decision Mr. Burnley went to work for a law firm for the express purpose of representing Eastern and Continental in transportation matters.

In sum, Mr. Lorenzo is not an airline builder. You cannot build a successful airline by feeding your employees a daily gruel of lies, threats and distortions. Indeed, in the long run you cannot build anything worthwhile on a structure of fractured promises and broken commitments. Congress cannot make Frank Lorenzo an enlightened employer, but it can take action to prevent him from looting Eastern to suit his own private interests. Congress should take such action immediately.

REMARKS SUBMITTED FOR THE RECORD
BY CAPTAIN JOHN J. BAVIS
CHAIRMAN, MASTER EXECUTIVE COUNCIL
EASTERN AIR LINES
AIR LINE PILOTS ASSOCIATION
BEFORE THE
SUB-COMMITTEE ON AVIATION
COMMITTEE ON PUBLIC WORKS AND TRANSPORTATION
U.S. HOUSE OF REPRESENTATIVES
JUNE 29, 1989

From the moment they first become involved in aviation, pilots are trained to play by the rules. Aviation, like almost no other profession, is terribly unforgiving of those who violate the rules and attempt to march to a different drummer. Rules are made to be obeyed.

That respect for order and discipline carries over into our lifestyles as well. As a group, a higher percentage of us are non-smokers, a higher percentage of us exercise regularly, a higher percentage of us are mentally well-adjusted than almost any other profession in America. We play by the rules.

We behave the same way when it comes to dealing with our respective managements. We follow the blueprints for sociallyacceptable behavior that have been painstakingly built up over the years. We negotiate contracts with our companies and work within the scope of those contracts until it is legally possible for us to re-negotiate the terms of our working agreements. We set up grievance machinery in conjunction with our companies so that all parties can seek redress for contractual violations in an orderly, non-disruptive manner. And we deliver to our managements an honest day's work for an honest day's pay. We play by the rules.

The social contract that is the bedrock of the American way of life pre-supposes that justice is administered fairly and without prejudice and that nobody is given preference over another because of social status, ability to pay, or influence in the community. That is why the Goddess of Justice is depicted as blindfolded, with balanced scales in one hand and a sword in another.

Those who play by the rules have nothing to fear from this concept of justice for it assures that the playing field will be even and that right will prevail. But because justice is blindfolded it is often easy for the unscrupulous to put a finger on the scale without being detected, thus tipping the delicate balance unjustly in favor of the cheat and penalizing those who play fair.

We, the employees of Eastern Air Lines, are faced with such a dilemma today. We have consistently played by the rules in our dealings with management, only to see influence and technicalities prevail to our disadvantage. Sorry to say, the American system of justice has not been even-handed with regard to the situation at Eastern.

In February of 1986, in a highly-questionable midnight deal, the Board of Directors of our company sold the airline to Frank Lorenzo for far less than its real worth, thereby disenfranchising the 25% ownership by the employees. Eastern paid 57% of its own acquisition costs. The Board saw to it that no one other than Lorenzo would be allowed to bid for the airline. And a man who was in a financially precarious position with his other holdings, Continental Airlines, still in bankruptcy proceedings at that time, was allowed to purchase Eastern at a fire-sale price with hardly an eyebrow raised. This was the first confrontation between those who were taught to play by the rules and one who was taught that rules were made to be broken. Many more such confrontations would follow as Lorenzo systematically stripped assets from our airline and forced valuable employees to curtail their careers and leave the company rather than suffer the abuses that became the hallmark of the Lorenzo style of management.

Eastern's employee groups served as watchdogs as these unethical and illegal management moves occurred. But in our instance, the Goddess of Justice was not only blindfolded, she also wore earmuffs. Our cries for justice went unanswered.

We petitioned Congress to determine whether Texas Air was fit, willing, and able to manage Eastern Air Lines only to have the Department of Transportation pre-empt the pending investigation with an investigation of its own, followed by an exoneration of the company by the then Secretary of Transportation, who has since joined Texas Air's leading legal firm.

We asked the courts to investigate the multiple instances of asset transfers which were draining the very lifeblood from our company. In an unprecedented ruling Federal Judge Barrington Parker agreed that the airline was being systematically dismantled, but bought management's argument that it was trying to shrink its way to profitability - a concept that has long proven to be untenable in the airline industry. Judge Parker took management at its word with regard to the need for asset sales but warned it against perpetrating a "cruel hoax" on the

American public and the justice system if those sales were part of a larger scheme to bankrupt Eastern. Those words ring prophetically true one year later and speak volumes about the deception and duplicity of Frank Lorenzo and his management team.

We had been saying from the outset that Frank Lorenzo never had any intention of running Eastern as a profitable company. From the moment he took control, he began stripping billions of assets away in order to benefit Texas Air and Continental. To date, after 3 1/2 years, he has not invested one penny in Eastern.

From the time he finalized his purchase of Eastern, he also declared war on the employee groups, imposing onerous, unilateral sick leave and attendance policies in clear violation of our legally binding contract.

His management team began to remove pilots from trips when they refused to fly aircraft they didn't deem airworthy. He attempted to have us violate clear and well-established FAA regulations. He tried to have us look the other way while margins of safety were shaved. He declared that he would not recognize our legally-binding contract under the Railway Labor Act and forced us to go to court to have the sanctity of that contract preserved.

We tried to stop Lorenzo by working within the system...by playing by the rules. We spent millions of dollars in court proceedings battling Lorenzo's army of lawyers. We came to Congress on eight separate occasions seeking assistance. We provided mountains of documentation to the FAA and the DOT in support of our charges. We spent many hours at the negotiating table attempting to work with management to put Eastern back on a profitable, competitive course.

And finally, after three exhaustive years in which we saw one door after another close in our face, we took the ultimate step of stopping work in a legal sympathy strike under the Railway Labor Act. It was not a strike by a few diehard militants -- over 95% of Eastern's pilots voted to support the strike. Nor was it a strike for higher wages. On the contrary, Eastern's employee groups offered unprecedented concessions to any ownership group that would step forward and release our airline from the destructive death grip of Frank Lorenzo. Over 25,000 Eastern employees have voted with their feet in an amazing show of resolve to protest the ownership of our airline by Frank Lorenzo. If we were somehow magically transported to Tiananmen Square, we would have been applauded for our courage and determination. If we were Polish shipyard workers we would be hailed for our Solidarity. In modern day America, we have been ignored.

We have tried to make the system work. We have played by the rules. But, sad to say, the system has not served us well. Frank Lorenzo has demonstrated repetitive non-compliance with existing FAA rules and regulations. He has not been penalized for these chronic violations.

Frank Lorenzo won administration approval for his proposed plan to be a major, competitive leader in the airline industry, but he has cut capacity at every turn, thereby reducing competition and giving dramatic price advantage to other carriers who have become dominant in their individual marketplaces. Lorenzo downsized, drained the profits, and suffered no penalty for this deception.

Lorenzo plays the American judicial system like a violin, operating on the theory that he can bend and manipilate the law with impunity. If you catch me, fine me. If you catch me, sue me. No matter what you do, you can't stop me. So far, I see no evidence to prove that theory wrong.

Contrast that with the manner in which the system has treated the workers -- the pawns in the high-flying greed that personifies

Lorenzo's modus operandi.

The President became the first in our history to refuse to enpanel a Presidential Emergency Board to help adjudicate labor negotiations as requested by his own National Mediation Board -- the first refusal out of 216 similar requests.

The Congress has passed no definitive legislation to stop Lorenzo, even though strong expressions of support for our cause have been forthcoming from individual members.

The FAA seems to consider its job to be one of reassuring the public and protecting airline management, whether or not that management is deserving of the public trust.

The DOT talks about the value of competition, but stands idly by while Lorenzo, owner of Continental, dismantles his own competition.

In the courts, Lorenzo is being allowed, under the guise of bankruptcy, to liquidate Eastern, even though that is not the alternative which best serves the interests of the nation, the employees, the creditors, or the communities which Eastern serves.

We have worked within the system. We believed in the American dream. But the system has failed us up to now, and the dream has turned into a nightmare.

As the elected representatives of the American public, you have it within your power to prove that the scales of justice can be balanced. You have the evidence. Frank Lorenzo can not be allowed to get away with his "cruel hoax" any longer. Now is the time for all of us who play by the rules to call Frank Lorenzo to task and remove his thumb from the scales of justice.

Mr. **Oberstar**. Next, we have the Transport Workers Union President, Mary Jane Barry. Thank you very much for being with us and for your patience throughout this very long, interrupted day. And yet on a matter of very great importance to you, to your membership, and to the traveling public. Please proceed as you wish. We have your prepared statement which will be included in the record. You may summarize it or deliver in full, as you choose.

TESTIMONY OF MS. MARY JANE BARRY, PRESIDENT, TRANSPORT WORKERS UNION, LOCAL 553, ACCOMPANIED BY PENNY PILZER, JUDY COUGHLIN AND NANCY CURRIER TAUSS

Ms. **Barry**. Thank you. My name is Mary Jane Barry and I am the President of TWU Local 553. TWU represents close to 6,000 Eastern Air Lines Flight Attendants. The Flight Attendants have been engaged in a sympathy strike for more than three and one half months against Eastern Air Lines.

The personal toll that the strike has taken on the members of my union and the many good reasons for which they took their stand have been explored in the press and elsewhere. In 1986, the flight attendants agreed to make a 20 percent concession in wages and wage-related items in our contract. The same day concessions were made, Eastern was sold to Texas Air. Texas Air thanked us for our cooperation by asking us for an additional $69 million in concessions. I am here to ask that the efforts and sacrifices of my members, who were willing to cooperate, and when they failed, to take their lumps in an economic war, not to be thwarted because it has not been a fair fight.

Captain Duffy has highlighted for you some of the ways in which Texas Air has created Eastern's insolvency. Now the insolvency is being used to frustrate employee rights normally protected under the labor and transportation laws and to nullify the tools which labor traditionally uses to negotiate and settle labor-management disputes—to the detriment of the flying public.

An obvious example of the way in which bankruptcy under Chapter 11 distorts the traditional balance maintained by our labor laws is one of raw economics. Our members must pay their bills notwithstanding the strike. Texas Air by contrast, has used the bankruptcy proceedings to stave off its creditors, thereby enhancing its ability to wait its employees out.

Another fundamental labor tenet is that the employees' right to negotiate and enforce collective bargaining agreements. Eastern has informed us that it wishes to modify our existing collective bargaining agreement. Of course we will do our best to reach an agreement with Eastern. But Eastern's position is that if we do not, we will not have recourse to the National Mediation Board or the Presidential Emergency Board, which possesses the expertise to mediate and fairly decide such matters. Rather, Eastern says, collective bargaining issues will be brought before a bankruptcy judge who by training and experience could not be expected to have expertise in labor matters, but who will decide which modifications are necessary to Eastern's reorganization.

If this is a true rendition of the law, we will have been deprived not only of our agreement, but even of the opportunity to negotiate one. Already, we have been deprived of the right to enforce our agreement. The stay in bankruptcy prevents the processing of the many legitimate grievances employees and their unions have against the company.

Even more disturbing than the way in which bankruptcy proceedings have rendered carefully constructed labor laws less potent is the cynical way in which Chapter 11 is being used here to further a plan of liquidation. As Mr. Kupersmith can further explain, Eastern's reorganization plan is nothing more than the slow liquidation begun when Texas Air first purchased Eastern. The projections on which the plan rests are fantasy at best—cynical and calculated lies at worse.

There can be no doubt that Eastern's current plan, which calls for selling off even more routes to other major carriers until for all practical purposes Eastern ceases to exist is clearly anti-competitive. The affect on the fares and routes available to the traveling public as fewer, larger carriers dominate the market is as predictable as it is adverse. Thus, the neat sidestepping of the country's labor laws and ultimate pillaging of a substantial and important corporation affects more people than just its employees.

Many of these problems could have been obviated had the President accepted this Committee's recommendation and formulated a Presidential Emergency Board to end this dispute. At that time, Eastern and the Secretary of Transportation Skinner contended that the Presidential Emergency Board would be too time consuming and would interfere with the bargaining process. I think it is worth noting that had the Committee's recommendation been signed into law, this dispute would have been over months ago and the flying public would have had another competitor in the marketplace.

The bankruptcy laws were never intended to be so cynically manipulated to this end. The labor laws were not enacted in order to be preempted in this fashion. Air transportation has not been regulated so that the regulators might turn a blind eye to the mismanagement and ultimate disappearance of a major carrier.

On behalf of my membership, I ask that Congress act to prevent the dissolution of public assets and regulating harm to the public weal. I thank you for the opportunity to address you, Mr. Chairman, today.

Mr. OBERSTAR. Thank you very much. Again, I apologize for the late hour, but as you can see, throughout the day the proceedings were interrupted by legislative business on the House floor. What role have the flight attendants played in negotiations with Mr. Ritchie?

Ms. BARRY. We have been in meetings with Mr. Ritchie on several occasions along with the other unions in joint discussions to cooperate in making the plan successful.

Mr. OBERSTAR. I neglected at the outset of your testimony to ask you to introduce for the record your associates, so that their names could be included in the record at this point. Would you please do that?

Ms. BARRY. Certainly. Penny Pilzer is our attorney. Judy Coughlin to my right is our secretary-treasurer. And Nancy Currier Tauss is our vice president.

Mr. **Oberstar**. Thank you. We have heard from Mr. Bakes that pilot training exceeds the amount of training that was occurring pre-strike and which other carriers are now providing for their pilots. What type of training is occurring for flight attendants?

Ms. **Barry**. They are training people that are very young and many of them are leaving the training class before they even finish. I think you are probably familiar with when TWA flight attendants had their strike, there was a Congressional hearing regarding the training and the necessity of also having experienced flight attendants, and not all new flight attendants flying on aircrafts.

Mr. **Oberstar**. Mr. Bakes also indicated that the new Eastern is hiring what he called experienced pilots. Of course, Captain Duffy addressed that better in his testimony indicating that they may have the hours, but they are certainly not experienced in the sense of the kind of experience one expects for an airline pilot. What do you know of the background of experience and qualifications of those people who are being hired as flight attendants for Eastern? Do they come out of the ranks of existing carriers or do they have any background at all?

Ms. **Barry**. The flight attendants they are hiring I do not think would leave another carrier to come over to Eastern, but I know that they are interviewing. They are having a difficult time hiring flight attendants because they are going into smaller towns. There are many airlines that are hiring in the airline industry and certainly too many want to come and fly with Eastern when airlines like United and Piedmont and U.S. Air are hiring.

I do not know that they have changed the training program per se. They have not really given me any of that information. I just know that they are very young and not experienced in the airline industry. They are not going from one carrier over to Eastern.

Mr. **Oberstar**. Are you providing the FAA with information as you receive it, that is, the TWU, about the status of these trainees, so that FAA can take cognizance of it and take whatever action may be appropriate?

Ms. **Barry**. We have a safety director who works for Local 553 and she is coordinating those things. She worked very actively with Representative Collins—she is from Illinois—when the TWA flight attendants' strike situation happened. And it is to be concerned about as well as pilots who are new in the field to have all new flight attendants on an aircraft is not a good safety service, we believe.

Mr. **Oberstar**. It certainly concerns me very greatly, just as we have discussed at some length the matter of pairing with pilots. If you have all flight attendants as part of a crew who are inexperienced, they are the first line of safety and safety will certainly be jeopardized on those flights to the extent that all inexperienced flight attendants are providing the service.

Ms. **Barry**. We share those same concerns.

Mr. **Oberstar**. I think it has to be emphasized the principal role of the flight attendant is the safety role, and as I said a moment ago, they really are the first line of safety on board aircraft and that has to be recognized. And if the new airline is going to be staffing its personnel with inexperienced, minimally qualified people, safety is going to be at risk.

Ms. **Barry**. I think that is everyone's concern to the public and we are very concerned and plan on staying on top of it.

Mr. **Oberstar**. Thank you very much for your testimony. I wish there were more we could offer in the way of concrete specific steps to be taken. We certainly will continue to pursue, that is, this Subcommittee will continue to pursue every possible avenue of support to bring Eastern back in its former configuration with those people who have given their careers and their lifetimes to service in that airline.

Ms. **Barry**. Thank you very much for your consideration. We know you will do everything you can do. Thank you.

[Ms. Barry's prepared statement follows:]

TESTIMONY OF
MARY JANE BARRY, PRESIDENT
TRANSPORT WORKERS UNION, LOCAL 553, AFL-CIO
ON THE EASTERN STRIKE

June 29, 1989

Good morning, my name is Mary Jane Barry and I am President of TWU Local 553. TWU represents close to 6,000 Eastern Airlines Flight Attendants. The Flight Attendants have been engaged in a sympathy strike for more than three and one half months against Eastern Airlines.

The personal toll that the strike has taken on the members of my union and the many good reasons for which they took their stand have been explored in the press and elsewhere. In 1986, flight attendants agreed to make a 20% concession in wages and wage-related items in our contract. The same day concessions were made, Eastern was sold to Texas Air. Texas Air thanked us for our cooperation by asking for an additional 69 million dollars in concessions. I am here to ask that the efforts and sacrifice of my members, who were willing to cooperate, and when that failed, to take their lumps in an economic war, not be thwarted because it has not been a fair fight.

Captain Duffy has highlighted for you some of the ways in which Texas Air has created Eastern's insolvency. Now that insolvency is being used to frustrate employee rights normally protected under the labor and transportation laws and to nullify the tools which labor traditionally uses to negotiate and settle labor-management disputes--to the detriment of the flying public.

An obvious example of the way in which bankruptcy under

Chapter 11 distorts the traditional balance maintained by our labor laws is one of raw economics. Our members must pay their bills notwithstanding the strike. Texas Air, by contrast, has used bankruptcy proceedings to stave off its creditors, thereby enhancing its ability to wait its employees out.

Another fundamental labor tenet is the employees' right to negotiate and enforce collective bargaining agreements. Eastern has informed us that it wishes to modify our existing collective bargaining agreement. Of course we will do our best to reach an agreement with Eastern. But Eastern's position is that if we do not, we will not have recourse to the National Mediation Board or the presidential emergency board, which possess the expertise to mediate and fairly decide such matters. Rather, Eastern says, collective bargaining issues will be brought before a bankruptcy judge who by training and experience could not be expected to have expertise in labor matters--but who will decide which modifications are necessary to Eastern's reorganization. If this is a true rendition of the law, we will have been deprived not only of our agreement, but even of the opportunity to negotiate one. Already, we have been deprived of the right to enforce our agreement. The stay in bankruptcy prevents the processing of the many legitimate grievances employees and their unions have against the Company.

Even more disturbing than the way in which bankruptcy proceedings have rendered carefully constructed labor laws less potent is the cynical way in which Chapter 11 is being used here to further a plan of liquidation. As Mr. Kupersmith can further explain, Eastern's "Reorganization" plan is nothing more than the slow liquidation begun when Texas Air first purchased Eastern. The projections on which the plan rests are fantasy at best--cynical and calculated lies at worse.

There can be no doubt that Eastern's current plan, which calls for selling off even more routes to other major carriers until for all practical purposes Eastern ceases to exist is clearly anticompetitive. The affect on the fares and routes available to the travelling public as fewer, larger carriers dominate the market is as predictable as it is adverse. Thus the neat sidestepping of the country's labor laws and ultimate pillaging of a substantial and important corporation affects more people than just its employees.

Many of these problems could have been obviated had the president accepted this committee's recommendation and formulated a presidential emergency board to end this dispute. At that time, Eastern and Secretary of Transportation Skinner contended that the Presidential Emergency Board would be too time consuming and would interfere with the bargaining process. I think it is worth noting that had the committee's recommendation been signed into law this dispute would have been over months ago and the flying public would have another competitor in the marketplace.

The bankruptcy laws were never intended to be so cynically manipulated to this end. The labor laws were not enacted in order to be preempted in this fashion. Air transportation has not been regulated so that the regulators might turn a blind eye to the mismanagement and ultimate disappearance of a major carrier. On behalf of my membership, I ask that Congress act to prevent the dissolution of a public asset and regulating harm to the public weal.

Mr. OBERSTAR. Thank you very much. Next, we have Mr. Patrick V. Murphy, Deputy Assistant Secretary for Policy and International Affairs of the Department of Transportation and Mr. John S. Kern, Deputy Associate Administrator for Regulation and Certification at FAA are our next witnesses. Mr. Murphy and Mr. Kern, welcome.

TESTIMONY OF A PANEL CONSISTING OF PATRICK V. MURPHY, DEPUTY ASSISTANT SECRETARY FOR POLICY AND INTERNATIONAL AFFAIRS, DEPARTMENT OF TRANSPORTATION; AND JOHN S. KERN, DEPUTY ASSOCIATE ADMINISTRATOR FOR REGULATION AND CERTIFICATION, FEDERAL AVIATION ADMINISTRATION

Mr. MURPHY. Thank you, Mr. Chairman. I would like to shorten my statement, but nevertheless present the highlights to you. I will go through as quickly as possible. I am pleased to be here today to discuss the Department of Transportation's activities in connection with Eastern's bankruptcy proceeding.

With me is Mr. Kern who will be available to address safety and readiness-to-operate issues involving Eastern Air Lines.

The Department has been monitoring closely the activities of Eastern Air Lines for some time. In April 1988, then Secretary of Transportation Burnley announced a preliminary investigation of Eastern, its sister company, Continental, and its parent, Texas Air Corporation. This investigation was launched to determine whether there was substantial cause to question the carriers' continuing fitness and whether they were disposed to comply with the safety and economic rules applicable to air carriers. As part of this investigation, the FAA commenced a special 30-day inspection of Eastern that was subsequently broadened to include Continental and its commuter subsidiaries.

On June 2, 1988, a final report was issued and the investigation was concluded. The results of the investigation showed that both Eastern and Continental continue to meet the Department's fitness standards with respect to management, finances, and compliance disposition. With respect to financial fitness, the investigation found that despite significant losses at both carriers, each had sufficient access to capital to operate safely without undue risk to the public.

The investigators did find that while Eastern and Continental had satisfactory compliance dispositions, the labor-management tension at Eastern raised concerns about the carrier's ability to comply in a full and satisfactory way with our safety requirements over the long term. As a result, Secretary Burnley asked former Secretary of Labor William Brock to work with Eastern's management and employees to build the lines of communication and cooperation within the company that are necessary to maintain the highest level of safety.

On July 6, 1988, Secretary Brock announced his efforts had resulted in a successful negotiation of an agreement between management and employees to establish procedures that would open lines of communication. Unfortunately, during the late fall of last year, the procedures established by the agreement broke down.

Eventually, as we all know, on March 4, 1989 there was a strike. Prior to the strike and the subsequent bankruptcy filing, the Department established a Strike Impact Center staffed by DOT personnel to collect and provide the Secretary with information on the economic effects of the strike by the IAM on Eastern, as well as on the operation of other major airlines and railroads, including commuter rail.

The FAA simultaneously established a separate center for monitoring the safety-related aspects of the strike. At least daily contacts with each of the major air and rail carriers, as well as Eastern unions, were maintained to determine whether secondary boycotts of other carriers had occurred, as well as whether any displaced passengers from Eastern's flights were not being accommodated.

Close monitoring of the strike situation was maintained through this center for 12 to 14 hours a day for almost three weeks. FAA monitoring was on a 24-hour basis for the same period of time. When it appeared that the major disruption in the transportation system would not likely occur, daily contacts, other than with Eastern and its unions, were discontinued.

Various factors served to moderate the initial impact of Eastern's service reductions on consumers. The potential strike had been well-publicized in advance, coming at the end of a 30-day cooling off period. Many travel agents and passengers had already made alternate travel arrangements. A number of carriers accepted Eastern's tickets when the strike began and several continued to accept them even after the bankruptcy filing. Major cruise lines arranged transportation on other airlines at no additional charge for package cruise customers with Eastern's tickets.

The Department's Consumer Affairs Office responded to telephone inquiries from affected travelers and issued a fact sheet immediately following the bankruptcy. That office has continued to track consumer problems on the carrier. Compared to the sudden bankruptcy of Braniff in 1982, the effects of the Eastern bankruptcy have been limited. Following Braniff's bankruptcy, the Civil Aeronautics .Board received 170 consumer inquiries per hour, whereas following Eastern's bankruptcy, we received only 131 inquiries for the entire month of March.

Since the first month of the strike, the number of complaints about Eastern reported to our consumer office has been very small. As a matter of fact, the number of complaints actually decreased sharply from 131 in March to 44 in April to 34 in May and 18 for the first three weeks in June.

As for the bankruptcy proceeding itself, the Department is not a direct party to that proceeding. But like other Government agencies having an interest in the proceeding, such as the Internal Revenue Service and GSA, we are represented in the case through the U.S. Attorney's Office in New York. We have been monitoring closely the issues raised and the decisions made by the Judge, particularly those that affect airline fitness or competition.

Our General Counsel's Office has been receiving and reviewing the documents filed and issued in the court. We have been carefully reviewing individual transactions resulting from the bankruptcy case and from Eastern's restructuring plan. To this end, we did not object to the sale of the Shuttle operation to Donald Trump, since his airline had already been found fit by the Department and had already been issued a certificate by the FAA.

However, when Eastern was proposing to sell certain gates at Philadelphia and two Canadian routes from that city to USAir, Secretary Skinner sent a letter to the Attorney General raising serious concerns about this sale on antitrust grounds, finding that the transaction would create significant competitive and international transportation policy problems. Subsequently, the Justice Department threatened that it would sue Eastern if the carrier proceeded with this sale. Eastern withdrew its agreement with USAir and has now agreed to sell those assets, as well as some aircraft, to Midway Airlines. This is expected to result in a major new hub in Philadelphia bringing new competitive service to the Northeast. The Department also welcomes the emergence of the Trump Shuttle with its plans to renew and revitalize the Eastern Shuttle operation.

Further, on June 13, Secretary Skinner sent a letter to the Chief Executive Officers of 28 air carriers reminding them of the provisions of Section 401(h) of the Federal Aviation Act, under which international route transfers are subject to prior Departmental approval. In that letter, the Secretary indicated that he viewed with concern the prospect that carriers might endeavor to sell these routes and that such sales might undercut important public benefits that the Department sought to achieve by awarding the routes in the first place. Recent press reports indicate that Eastern may be negotiating with American Airlines for the sale of certain of Eastern's Latin American routes. Any such sale, if actually proposed, will be subject to full DOT review.

In concluding my remarks, I want to you to know that the Department continues to monitor the Eastern bankruptcy and strike situation, providing periodic reports to the Secretary. The Department has continued to maintain regular contacts with the unions in order to keep in touch with the progress of the strike and bankruptcy from their point of view. The FAA is also continuing to scrutinize very closely Eastern's operations from the safety standpoint.

Mr. Chairman, this concludes my prepared statement.

Mr. **Oberstar**. Thank you, Mr. Murphy. I get the impression though from your testimony that while the Department is monitoring the bankruptcy case and looking after the antitrust issues, and whether it may raise any anti-trust issues, that you really do not have a handle on the big picture. You do not seem, at least satisfactorily to me, to address the issue of critical size, of critical mass, of whether the reduction of assets in this bankruptcy proceeding is proceeding to a point where it may not be possible for Eastern to emerge as a major carrier.

Have you reviewed the Eastern plan? Have you reviewed the Ritchie plan to determine which of them or either of them offers a good prospect for the emergence of Eastern as a viable competitor?

Mr. **Murphy**. Mr. Chairman, I think you have raised two questions. One, whether the Department is focusing on the big picture. The big picture meaning competition in the airline industry——

Mr. **Oberstar**. That is right.

Mr. **Murphy**. At an era, at a time, 10 years after deregulation. We have seen a large number of mergers. We are now faced with a leveraged buyout in one of our healthiest carriers. We are aware of other leveraged buyouts being considered, and I want to assure you that the Department is most concerned about the big picture. Our new Secretary Skinner has started a series of competition studies that will be done this year that are reviewing the airline industry from top to bottom. I am responsible for having those studies prepared. The Secretary is adamant that he do everything to preserve competition in this airline industry because without it deregulation will not work. Deregulation was based, as you know, on competition.

Mr. **Oberstar**. Does that include the consideration of legislative recommendations to strengthen the Department's hand, apart from antitrust on the one hand with the Justice Department and pulling the certificate of fitness on the other hand, which are two rather drastic actions that agencies may be reluctant to use?

Mr. **Murphy**. Yes. Mr. Chairman, the Secretary with the aid of our studies, I think, has kept an open mind on what remedies, if any, would be needed to make sure the airline industry remains competitive. I will speculate that those remedies could be regulatory, involving rules affecting things like computer reservation systems or slots, or they could be statutory. And as you know, the General Accounting Office and others have prepared studies that some members of Congress think might require some legislation.

With regard to the transactions that have been discussed today, the Department has not reviewed in a comparative way the proposals that are now before the court. Our view is that when the court approves a plan, or even before that when a plan is formally presented to the court, we will review that to ensure that that plan will result in a fit airline. But we have not taken the position that we will advise the court on which plan is the better plan. We have stayed out of that, and I think that will remain our position.

Mr. **Oberstar**. But when a specific plan is submitted, when the court has something before it, how will this operate? Will the court invite the Department's comments? Will the Department just simply take cognizance and involve itself?

Mr. **Murphy**. The Department does not wait for the court's invitation. When a plan is submitted, we will then subject that plan to our continuing fitness requirements under the statute. We will ensure that there is a viable financial plan, that there is viable management, that the people who will be involved in managing this company have a good compliance disposition, and that the plan is operationally feasible from an FAA standpoint and will result in a fit airline.

In addition, of course, today we have heard discussion about sales of assets, and I must say, I was struck by the almost cavalier way in which some of the sales of those assets were discussed—international routes—as if the Department of Transportation would merely rubber stamp a route sale. Something as large as the entire Latin American Division of Eastern Air Lines, I can assure you, just as the Philadelphia gate sale involving eight gates at Philadelphia, will be scrutinized very carefully. And even a larger transaction involving a whole division of Eastern Air Lines will be looked at extremely carefully, Mr. Chairman.

Mr. **Oberstar**. I am glad to hear that and that the Department will exercise vigorously that authority. I had intended to raise that question with the examiner. We just simply ran out of time, too many interruptions, but it is the Department's responsibility and authority to approve any such sale in the international routes area and I would expect that to be very carefully scrutinized and the Department to exercise the full range of its authority.

Mr. **Murphy**. We will, Mr. Chairman. I can assure you of that.

Mr. **Oberstar**. I am impressed with the Secretary's interest in aviation, with his desire stated many times to assure the continuation of competition. I was very pleased and impressed with his quick response to the proposed acquisition of Northwest Airlines. But there are some limitations on what the Department can do. There is a lot of jawboning and cajoling and public exposure proposals. It can be done by the Department, but there are at this point not many regulatory tools to use to slow down, adjust or modify in some way that type of action, and there seem to be very few tools available to the Department in the instant case pending in bankruptcy. So that the bankruptcy law becomes an abettor to the purpose of Mr. Lorenzo to downsize and remove a major carrier from national competition.

Mr. **Murphy**. Mr. Chairman, it is true that with the Deregulation Act, the Federal Government moved out of the business of formally regulating the airlines, and we do not have the tools in the Federal Government today that we had 10 years ago. But to date, we have not found that to have been a hindrance in monitoring and dealing with the airline industry. As far as the ultimate outcome of Eastern Air Lines, the idea that was put forward of critical mass as a 200-aircraft concept was a new concept to me. At the time the Deregulation Act was debated, economists talked about economies of scale and what would be the appropriate size to have an effective competitor, and at that time numbers like 10 aircraft and 20 aircraft were discussed. Today we certainly have a different industry with hubbing and with computer reservation systems, but I personally find it difficult to believe that we need a 200-aircraft airline to have effective competition out there.

Mr. Donald Trump started the Shuttle with 21 aircraft and we were delighted to see that. We were delighted to see Midway Airlines expand its size by 40 to 50 percent by starting a hub at Philadelphia, and yet it still will not be a 200-aircraft airline. So we believe that competition can still come out of the Eastern Air Lines restructuring.

Mr. **Oberstar**. Certainly Trump airlines is not a major carrier. They are not in the national class. That is more in the nature of a commuter regional operation—big in number and dollar amounts and number of passengers, but they are nowhere in the mold of pre-strike Eastern.

Mr. **Murphy**. That is absolutely correct. On the other hand, it does represent a new competitor in the industry and we have no reason to believe that Mr. Trump could not expand that airline. He certainly has the financial wherewithal to do that, and we are just delighted whenever we can have a new airline come into the business and stand out there as a potential competitor.

Mr. **Oberstar**. Now that you have learned the term critical mass, as many of us have in the course of this bankruptcy proceeding, are you going to be looking at this matter further in determining what is appropriate in various circumstances? These are matters to which the Department, it seems to me, must turn if it is going to address the matter of a national transportation policy and adequacy of competition in the airline industry. We would hope that you will do that in the course of the Secretary's direction to the Department.

Mr. **Murphy**. We certainly will be examining all types of competition in the industry and seeing whether various size of airlines have an inherent advantage. I will just point out that we certainly have many airlines today that are operating below the 200 aircraft level. They are certainly not the largest airlines, but they remain competitive, carriers like America West, Southwest Airlines and others. But we will be examining the sizes of airlines in our studies, Mr. Chairman.

Mr. **Oberstar**. I certainly hope you will do that and do it in the much broader sense. Southwest Airlines and others that you have mentioned and others that we could discuss are not competitors for American, Delta, Northwest, and certainly are not replacements for Eastern, and maybe Trump can grow into something, but it will take at least in the short term, a miracle of the loaves and fishes to do that.

The matter of public interest is a major concern. How, in your judgment, would the public interest be affected by the liquidation of Eastern and the sale of its assets to other airlines?

Mr. **Murphy**. Mr. Chairman, from a competitive standpoint, we would certainly hate to see the loss of a major carrier such as Eastern, an effective competitor, so that any breaking up of that is something we would not enjoy watching.

Mr. **Oberstar**. Would you do something about it?

Mr. **Murphy**. No, sir, I cannot state that we would. If those assets are spun off, as some already have been to Mr. Trump and to Midway Airlines, if they are spun off into other airlines in a competitive fashion, then competition can result and the public interest could be served by those assets being redeployed to other companies. It is not something we look forward to, but competition can still result from that outcome.

Mr. **Oberstar**. You are a little more optimistic than I am. I think, in the real world Mr. Lorenzo is going to proceed, and it appears to me that the court is going to permit him to proceed with this downsized airline and somehow hoping to grow it, as the term goes, into a larger entity. Has the Department done any analysis of the effect of this smaller airline on competition in the markets served on service and fares?

Mr. **Murphy**. We have not. Again, we are awaiting the plan. I noted today as the hearing was going on that this downsized Eastern, based on the back of the envelope calculations that I made, would appear to be an airline that might be in the size range of the present Piedmont Airlines and certainly that is an effective competitor, an airline that provides real competition in the United States. We will watch that.

Mr. **Oberstar**. Piedmont is making money though, is it not?

Mr. **Murphy**. It is, and presumably a downsized Eastern, if we can believe what we have heard today, will be a more efficient airline and one that at least the court has found can be a viable entity.

Mr. **Oberstar**. I guess time will tell, but up till now, it is also going to be run by the same fellow that could not make money at Continental and was not able to make money at the larger Eastern.

[Applause.]

Mr. **Oberstar**. Mr. Kern, I was troubled and I suspect you were by the testimony that we heard about pilots being hired and trained by the new Eastern. Do you review their training plan and what is underway and are you satisfied that they are meeting standards? That they are going to meet the FAA's recommendation about preparing of pilots?

Mr. **Kern**. Mr. Chairman, early on in the post-strike era we demonstrated our concern by a total review of the training programs at Eastern Air Lines. You heard today that the pilots now are receiving more training in terms of total hours than previously. We, in fact, have expanded the pilot training program to what I would call a 100 percent by the regulatory book program with no reductions, no shortcuts. That results in a much expanded training program.

The thing that I think is important for the Committee and for others to recognize is that the basic regulatory requirements, the standards that people must meet in order to fill the various seats in the aircraft certainly have not changed. And we would like to make sure that the Committee is comfortable with the fact that each and every person that goes through that program has to meet the same standards that have been tested over the 25 or 30 years, but with an expanded program.

Another thing that we changed that I hope will give you more confidence in their training program is that virtually every certification check that is given now at Eastern Air Lines is given by an FAA inspector. That is not common in the industry. We have many designees who work on behalf of the Administrator with virtually every other carrier. In fact, before the strike at Eastern, we had designees who did certification work on behalf of the Administrator. That is no longer the case at Eastern. The FAA has absorbed that workload.

I think the Committee can be comfortable with the product that is coming out of there. We certainly are.

Mr. **Oberstar**. You heard the discussion about the plan to operate in August and the targets. Are you satisfied those targets can be met?

Mr. **Kern**. I guess, I am in a very fortunate position. I have heard the targets. I have been well briefed on the plans of the company. The FAA early on was brought in to see these ambitious plans, mainly to make sure that we had our resources ready and our programs ready to accommodate them. But we do not have to really abide by those plans. Our interest is in the quality of the product at the end of the plan. If because of a higher than normal attrition rate or failure rate, they are not able to meet that plan, so be it. The plan will be slowed down.

I want to make sure the Committee is aware of the fact that we have continued our historical high degree of surveillance at Eastern Air Lines. We have totally revised the training program and conducting the check rules in Miami right now. And I do not mean to indicate an insensitivity of the plans of Eastern Air Lines, but the fact of the matter is the FAA's job is to make sure that the pilots, the flight attendants and the mechanics that ultimately reach the end of those programs are well equipped to do their job.

Mr. **Oberstar**. You know that the public is counting on you to do that job, to protect that safety, to ensure the margins of safety, and we know that the FAA has the capability to do it. And I am glad to hear that you have the will to do so, including the will to slow down their plan and slow down their operation, if necessary.

Mr. **Kern**. We made that clear early on. I would also like to address the issue of crew pairing that was discussed here today. Again we had early discussions with Eastern Air Lines knowing that it would be a factor that would come into play late in the summer. I have personally met with the chief operating officer of Eastern Air Lines. The head of our certificate management office in Miami and our regional division manager in Atlanta who are here with me today, have met with the officials at Eastern Air Lines. We have informed them, without question, that they would be expected to abide by the crew pairing rules that we established subsequent to that unfortunate accident in Denver.

Mr. **Oberstar**. Are you going to be taking the same cognizance of training of flight attendants?

Mr. **Kern**. Yes, sir.

Mr. **Oberstar**. I know what it takes in terms of resources, staff resources, to do that kind of inspection. I remember four years, almost five years ago, around the clock on Galaxy Airlines and the rather substantial number of personnel it took to make sure that one-horse airline did not kill any more people. Your surveillance of Eastern now, I understand, is taking a fairly sizable percentage of your inspector force in the Southeast region. You have got hundreds of other certificates to oversee. Do you feel that Eastern may be stretching FAA's resources too thin in that area?

Mr. **Kern**. We of course try to prioritize our work force where we need it. And it is, as you know, not up to strength and we appreciate this Committee's support in helping us get additional inspectors. But the situation in Miami right now with Eastern is our first priority in the Southern Region. We will make sure that the resources are allocated in order to provide for safe certification of the pilots as well as carefully watching over flight attendants and mechanics the training programs.

Mr. **Oberstar**. We have discussed the pilot side. We have discussed the flight attendants. What about the mechanic side? What kind of people is the new Eastern bringing in to do the maintenance work? And you remember very well our rather heated hearings on maintenance and Mr. Kolski of Eastern at the time?

Mr. **Kern**. Yes, sir, I do. I do not know that the maintenance program—maybe it is fair to say that it has not been tested yet. You heard testimony earlier today that there are an excess of aircraft available for use at Eastern Air Lines right now. Primarily their maintenance is being accompanied by veterans of Eastern Air Lines, people who were supervisors for years and years who are now back working on the aircraft.

Mr. **Oberstar**. It was said, I have not had grease on my hands in years. Does that make you feel awfully good about——

Mr. **Kern**. There was one story that I think got too much play about an attorney—apparently attorneys do not get grease on their hands very often, but that was an aberration.

Mr. **Oberstar**. I hope so. I want you to put a microscope on them. I have nothing but the most painful memories of the maintenance program at Eastern in our hearings.

Mr. **Kern**. We, of course, lived through those times together, Mr. Chairman, and the FAA, resource-wise, has undoubtedly expended a fair share, if not more on Eastern Air Lines. We have estimated that we probably spend 40 to 50 employee years on Eastern Air Lines every year, and relative to the effort on the other carriers—some larger, some smaller—that is extraordinary.

Mr. **Oberstar**. It certainly is and even in the good times, if those were indeed good times, when they had full complement of mechanics, and they had years long experience personnel, there were problems. There was a corporate culture problem at Eastern. I have no reason to believe that it would be substantially different in the future. And it is going to take continuous surveillance by the FAA to assure that safety is sustained, not at the margin because you have heard me say many times, not the least possible cost safety, but safety to the highest possible degree. That is, I know your commitment. That is what the law says. That is what the FAA has always attempted to achieve, even when it has been understaffed. And I just want to say that I have the highest respect for this agency and the morale of its people and the competence of its personnel. And I want to make sure that you put these folks under a microscope and watch them closely. The public depends on you.

Mr. **Kern**. Yes, sir.

Mr. **Oberstar**. Thank you very much. I appreciate your patience throughout this long day and your very valuable testimony.

Mr. **Kern**. Thank you.

[Mr. Murphy's prepared statement and responses from the Federal Aviation Administration [Mr. Kern] to supplemental questions submitted by Hon. John Paul Hammerschmidt follow:]

STATEMENT OF PATRICK V. MURPHY, JR.
DEPUTY ASSISTANT SECRETARY FOR
POLICY AND INTERNATIONAL AFFAIRS
DEPARTMENT OF TRANSPORTATION
BEFORE
THE HOUSE SUBCOMMITTEE ON AVIATION
REGARDING EASTERN AIR LINES

JUNE 29, 1989

Mr. Chairman and Members of the Subcommittee, I am pleased to be here today to discuss the Department of Transportation's activities in connection with Eastern's bankruptcy proceeding.

With me from the Federal Aviation Administration is Mr. John S. Kern, Deputy Associate Administrator for Regulation and Certification. Mr. Kern is available to address the safety and readiness-to-operate issues involving Eastern.

The Department has been monitoring closely the activities of Eastern Air Lines for some time. In April 1988, then Secretary of Transportation Jim Burnley announced a preliminary investigation of Eastern, its sister company, Continental Air Lines, and its parent, Texas Air Corp. This investigation was launched to determine whether there was substantial cause to question the carriers' continuing fitness and whether they were disposed to comply with the safety and economic rules applicable to air carriers. As part of this investigation, the FAA commenced a special thirty-day inspection of Eastern that was subsequently broadened to include Continental and its commuter subsidiaries.

On June 2, 1988, a final report was issued and the investigation was concluded. The results of the investigation showed that both Eastern and Continental continued to meet the Department's fitness standards with respect to management, finances, and compliance disposition. With respect to financial fitness, the investigation found that, despite significant financial losses at both Continental and Eastern, each carrier had sufficient assets and access to capital to operate safely and without undue risk to the public, and there did not appear to be any significant question about their financial viability for the near term.

The investigation did find that, while Eastern and Continental had satisfactory compliance dispositions, the labor-management tension at Eastern raised concerns about that carrier's ability to comply in a full and satisfactory way with our safety requirements over the long term. As a result, Secretary Burnley asked former Secretary of Labor William Brock to work with Eastern's management and employees to build the lines of communication and cooperation within the company that are necessary to maintain the highest level of safety. In addition, the FAA announced that it would increase its surveillance of Eastern to ensure that the carrier's operations were being conducted in full compliance with all safety requirements. On July 6, 1988, Secretary Brock announced that his efforts had resulted in the successful negotiation of an agreement between Eastern's management and its independent employees and unions to establish procedures that would open lines of communication within the company and would address the safety issues identified in the investigation. Unfortunately, during the late fall of last year, the procedures established by that agreement broke down.

Labor-management relations problems at Eastern culminated in a strike against the carrier by its Machinists union on March 4, 1989. Machinist picket lines have been honored by the majority of Eastern's pilots and flight attendants. As a result of the strike, Eastern curtailed substantially its service, initially being able to operate only about 10 percent of its flights. On March 9, Eastern sought protection from its creditors in the bankruptcy court under Chapter 11 of the U.S. Bankruptcy Code. Eastern is now under the protection of that court until the bankruptcy proceeding before the court is terminated.

Various factors served to moderate the initial impact of Eastern's service reductions on consumers. The potential strike had been well-publicized in advance, coming at the end of a 30-day National Mediation Board cooling off period. Many travel agents and passengers had already made alternate travel arrangements. A number of carriers accepted Eastern's tickets when the strike began, and several continued to accept them even after the bankruptcy filing. Major cruise lines arranged transportation on other airlines at no additional charge for package cruise customers with Eastern tickets.

The Department's Consumer Affairs Office responded to telephone inquiries from affected travellers and issued a fact sheet immediately following the bankruptcy advising Eastern customers of alternatives available to them. That office has continued to track consumer problems at the carrier. Compared to the sudden bankruptcy of Braniff in 1982, the effects of the Eastern bankruptcy on consumers were limited. Following Braniff's bankruptcy, the Civil Aeronautics Board received 170 inquiries per hour from consumers, whereas following Eastern's bankruptcy, we received only 170 inquiries for the entire month of March. Since the first month of the strike, the number of complaints about Eastern reported to our consumer office has been very small. As a matter of fact, the number of complaints actually decreased sharply -- from 131 in March to 44 in April, 34 in May, and 18 through the first three weeks of June. Refund problems accounted for one-half of those complaints, but in absolute numbers, the volume of complaints has been quite low.

Let me describe briefly for you the most important aspects of Eastern's refund practices.

Passengers holding Eastern tickets have several options. Under federal credit law, most people who bought Eastern tickets with a credit card are entitled to a refund from their credit card company. Eastern recently estimated that about 60 percent of its outstanding pre-bankruptcy tickets were credit card sales.

Eastern has created the Ticket Holder Assistance Program, under which passengers can apply their tickets as partial credit toward new Eastern flights. Continental Air Lines also initiated a program to offer full credit toward Continental tickets for Eastern tickets that were purchased from a travel agency. We understand that Eastern is not providing refunds for tickets purchased on or before the March 9, 1989, bankruptcy filing, because such refunds would be contrary to the requirements of the bankruptcy code.

Based on the consumer complaints filed with the Department, it does not appear that passengers are having difficulty in finding alternatives to the cancelled Eastern flights. This probably reflects the very competitive nature of Eastern's system.

Although several proposals to purchase Eastern from its current owners have been made, to date none of these attempts have been successful. At the present time, there is no formal restructuring program before the bankruptcy court.

On April 24, Eastern announced informally a plan for the restructuring of the airline. Under the plan, Eastern would sell about $1.8 billion in assets, including 98 of its 255 aircraft, 117 of its 281 gates, 28 of its 204 takeoff and landing slots (in addition to the 92 slots used in the shuttle operation), and certain unspecified international routes. Included in the plan was the sale of the Washington-New York-Boston shuttle operation to Donald Trump for $365 million, which has since occurred. Eastern proposes to rebuild a smaller airline, operating to 77 cities, compared to 102 before the strike, with 157 aircraft and 17,000 employees. The carrier indicated that it would concentrate on rebuilding its Atlanta hub and on adding flights on routes from the Northeast to Florida and the Caribbean, and that it could have 30 percent of its proposed service in place by July, 50 percent by August, and 100 percent by the end of the year. Proceeds from the asset sales would be used to pay off $914 million in debt. The remainder would be for working capital. Under Eastern's plan, fares would be discounted heavily during the rebuilding phase to lure back passengers.

Eastern apparently has reached agreements to sell almost $900 million in assets. This is about half of its goal of $1.8 billion. Included in these asset sales are the shuttle to Donald Trump; various assets, international routes, and facilities at Philadelphia to Midway Airlines; and certain aircraft.

The Department is not a direct party to the bankruptcy proceeding, but, like other Government agencies having an interest in the proceeding, such as the IRS and GSA, is represented in the case through the U.S. Attorney's office in New York. We have been monitoring closely the issues raised and the decisions made by the

Judge, particularly those that may affect airline fitness or competition. Our General Counsel's office has been receiving and reviewing the various documents filed and issued in the bankruptcy proceeding. We have been carefully reviewing individual transactions resulting from the bankruptcy case and from Eastern's proposed restructuring plan. To this end, we did not object to the sale of the shuttle operation to Donald Trump, since his airline had already been found fit by the Department and issued an operating certificate by the FAA. However, when Eastern was proposing to sell certain gates at Philadelphia and two Canadian routes from that city to USAir, Secretary Skinner sent a letter to the Attorney General raising serious concerns about this sale on antitrust grounds, finding that the transaction would create significant competitive and international transportation policy roblems. Subsequently, the Justice Department threatened that it would sue Eastern if the carrier proceeded with this sale. Eastern then withdrew its agreement with USAir and has now agreed to sell those assets, as well as some aircraft, to Midway Airlines. This is expected to result in a major new hub in Philadelphia bringing new, competitive service to the Northeast. The Department also welcomes the emergence of The Trump Shuttle with its plans to renew and revitalize the Eastern Shuttle operation.

Further, on June 13, 1989, Secretary Skinner sent a letter to the Chief Executive Officers of 28 air carriers reminding them of the provisions of section 401(h) of the Act, under which international route transfers are subject to prior Department approval. In that letter, the Secretary indicated that he viewed with concern the prospect that carriers might endeavor to sell these routes and that such sale might "undercut the important public benefits that the Department sought to achieve by awarding the route in the first place." Recent press reports indicate that Eastern may be negotiating with American Airlines for the sale of certain of Eastern's Latin American routes. Any such sale, if actually proposed, will be subject to DOT review.

Eastern now operates 79 flights a day to 27 destinations. By July 2, it hopes to fly 226 flights a day to 49 cities, and by August 1 it will add another 165 flights and 21 cities, bringing its service to 70 cities and 391 flights a day systemwide. Eastern has 6,000 employees now and by August 1 plans to add another 6,500 employees. By early 1990, the carrier hopes to have 17,000 employees on its payroll. Whether Eastern is able to succeed with its plans depends to a large extent on whether it is able to attract and hire new employees to conduct its operations, and whether its product will be attractive to consumers.

Prior to the strike and the bankruptcy filing, the Department established a Strike Impact Center, staffed by DOT personnel, to collect and provide to the Secretary information on the economic effects of the strike by the IAM on Eastern as well as on the operations of other major airlines and railroads, including commuter rail. The FAA simultaneously established a separate center for monitoring the safety-related aspects of the strike. At least daily contacts with each of the major air and rail carriers, as well as with Eastern's unions, were maintained to determine whether secondary boycotts at other carriers had occurred, as well as whether any displaced passengers from Eastern flights were not being accommodated. Close monitoring of the strike situation was maintained through this Center for 12 to 14 hours a day for almost three weeks. FAA monitoring was on a 24-hour basis during this same period. When it appeared that major disruptions in the transportation system were not likely to occur, the daily contacts, other than with Eastern and its unions, were discontinued.

In concluding my remarks, I want you to know that the Department continues to monitor the Eastern bankruptcy and strike situation, providing periodic reports to the Secretary on major developments. The Department has continued to maintain regular contacts with the labor unions in order to keep in touch with the progress of the strike and bankruptcy from their point of view. The FAA is also continuing to scrutinize closely Eastern's operations from the safety standpoint. My colleague, John Kern, will be able to speak to FAA's role.

Mr. Chairman, this concludes my prepared statement. I will be happy to answer any questions the Subcommittee may have on this matter.

CHRONOLOGY OF FAA SURVEILLANCE ACTIVITIES OF EASTERN AIRLINES
DECEMBER 1985 - MAY 1989

December 1985 - December 1986	Indepth Inspection. Findings revealed numerous regulatory violations.
March 1986	$9.5 million Civil Penalty.
June 1987	Eastern Region Special Surveillance Program.
Spring 1987 - Spring 1988	ALPA Postcard Review. 1305 cards were reviewed.
August 1987 - November 1987	Followup evaluation of 1985/86 Indepth Inspection by the Technical Evaluation Office (ASO-230).
April 1988	$823,000 Civil Penalty.
April 1988	FAA press release announcing special investigation, which among other things expressed concern with some of EAL's management practices.
February/ March 1988	Technical Services Review, conducted.
April/May 1988	Special 30-day ramp inspections conducted on EAL.
April/May 1988	Administrator formed a 6-man team of FAA Senior Executive Service personnel to analyze FAA/airline relationships.

April 1988	Secretary Burnley directed an indepth review of Texas Air Corp. and EAL's financial circumstances.
September 1988	EAL employees provide information of falsification of aircraft maintenance records at JFK.
March 4, 1989	EAL employees on strike.
May 1989	Based on findings EAL's maintenance facility at JFK was removed from their Operations Specifications.

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U.S. Department
of Transportation
**Federal Aviation
Administration**

800 Independence Ave., S.W.
Washington, D.C. 20591

August 22, 1989

The Honorable John Paul Hammerschmidt
House of Representatives
Washington, DC 20515

Dear Mr. Hammerschmidt:

This is in response to your July 14 letter regarding the hearing on Eastern Air Lines (EAL) on June 29. Our response to each of your questions follows.

1. What changes, if any, has the FAA noticed in Eastern's regulatory compliance posture since the strike started? To what would you attribute these changes?

ANSWER: Since the strike, top management of Eastern Airlines has exhibited a more compliant attitude toward its regulatory safety responsibilities in its public statements, in communications addressed to the EAL work force, and in meetings between FAA and company officials. This change may be the result of concerns expressed by the flying public and the unions, media attention, and Congressional interest as shown by the June 29 hearing and earlier hearings on Eastern's compliance posture. The continuing involvement of the FAA in monitoring the status of EAL's compliance with the Federal Aviation Regulations (FAR), including giving all post-training flight checks (until very recently), our ongoing enforcement investigations and civil penalty actions, and the agency's ongoing certification review incident to EAL's effort to bring a smaller airline out of bankruptcy, also may well have contributed to this attitude. Where the FAA has required or suggested changes to Eastern's procedures, top management of Eastern has been receptive and responsive.

2. Although it is operating a much smaller schedule today than before the strike, how would you compare Eastern's present maintenance procedures with those of other major carriers?

ANSWER: EAL's present maintenance procedures are comparable in nature to other carriers having equivalent aircraft, fleet size, utilization rates, and operating environments. Each of these factors must be considered when approving maintenance procedures for an operator. While the company now operates fewer maintenance facilities than before, its basic approved maintenance program has not changed significantly since the strike.

3. Charges have been made that EAL is being dismantled. Is their training program and general operation consistent with a plan to dismember the company? Is the maintenance and training program that they are undertaking very costly?

ANSWER: Although the first part of your question involves matters not generally within the province of the FAA's oversight responsibility, we have consulted with the Office of the Secretary of Transportation, and that office has provided the following information: The Reorganization Plan filed by Eastern with the Bankruptcy Court on July 21 did not include a disclosure statement, which would have described Eastern's proposed business plan and provided information relevant to its intended operations. (This statement is to be submitted to the Court on or before September 15.) However, the Plan did indicate that the business plan to be set out would not be "materially variant" from the preliminary plan proposed by Eastern's management in April. Eastern proposed at that time to downsize its operation to one serving 77 cities with 17,000 employees, and to concentrate on rebuilding its Atlanta hub and routes from the Northeast to Florida and the Caribbean. It would serve approximately 75% of the cities served before the strike, with a fleet of 157 aircraft or 62% of its prior total. This downsizing was stated in April as being premised upon the sale of about $1.8 billion in assets, although a recent filing increases that figure to $2.1 billion. Eastern has indicated that these sales are necessary for the company to continue operations and successfully reorganize, and such sales are, of course, subject to review and approval by the Bankruptcy Court and thus scrutiny by Eastern's creditors.

Eastern has entered into two major asset sales agreements during its reorganization effort. The first is for gates and other properties at Philadelphia, two Canadian routes, and 16 aircraft to Midway Airlines; the other was for the Eastern Shuttle properties to Trump Shuttle, Inc.

Eastern's stated plans are thus for downsizing, not for liquidation. Based on its service resumptions and other indicators of progress in its rehabilitation efforts, DOT cannot say at this time that these stated plans are unrealistic.

A fully informed judgment on Eastern's Plan cannot be made until the Disclosure Statement is submitted. We will be carefully reviewing the complete Plan to determine whether it presents a feasible approach, whether it would have any adverse effects on competition, safety, the firm's fitness to operate, etc.

While the FAA is not in possession of figures indicating EAL's expenditures on maintenance and training since the strike began, a considerable investment appears to have been made in hiring and training new pilots and maintenance personnel to replace those who have gone out on strike.

4. What is your assessment of the commitment of Eastern's management to continued compliance?

ANSWER: As outlined in the response to Question 1, EAL management appears to be committed to improve its record of regulatory compliance. In our meetings with the company, top management has indicated its support for changes requested by the FAA. Management has communicated to its work force the importance of complying with approved procedures and the FAR. At this point, we have uncovered no regulatory violations occurring after the strike began which give reason to question Eastern's capability for, or commitment to, regulatory compliance.

5. If Eastern were sold and most of the present management replaced, would the FAA or DOT insist on a "re-certification" or fitness review process to ensure that the new management was capable of operating the airline safely? Could the airline be allowed to operate until this process was completed?

ANSWER: If Eastern were sold and most of the present management replaced, the FAA would require certification of the new operator and the Office of the Secretary of Transportation (OST) would conduct a fitness review of the company. All air carriers are under a continuing statutory responsibility to remain fit. The Department can institute an investigation at any time to determine whether that responsibility has been met. The Department can also take such steps as are necessary to ensure that the carrier is operating safely and in accordance with all relevant safety requirements. Insofar as safety certification is concerned, the FAA requires that a new certificate be issued where an air carrier is sold and its management replaced. Certification of the new operator could range from a fairly simple administrative task to a complex, time-consuming process, depending on the nature and scope of the changes involved. Often appropriate measures can be taken in such cases to allow continuation of operations during transition of ownership.

6. Most of Eastern's mechanics are on strike. Are the employees now doing Eastern's maintenance properly licensed? Are they as qualified as the striking mechanics?

ANSWER: Eastern maintenance personnel must be appropriately licensed, qualified, and authorized to perform maintenance. This is required both by regulation and provisions contained in the company's General Maintenance Manual. Supervisory personnel are still responsible for the proper performance and signoff of work. The current mechanics at Eastern are properly licensed and meet the same regulatory qualification requirements as their predecessors.

7. We are told that the supply of qualified pilots is tight, yet Eastern says it is able to hire enough pilots to meet its needs. Are the pilots that Eastern is hiring and training fully qualified and experienced?

ANSWER: The pilots who have been hired by Eastern possess the appropriate FAA certificates and ratings. The minimum qualifications of each pilot meet or exceed FAA regulatory requirements and EAL's own requirements. The appropriate experience level above the FAA requirements is governed by EAL policies and practices. After the strike and up until very recently, the FAA conducted all post-training certification checks for new EAL pilots prior to their release for line operations, in order to assure that the training program maintains the highest level of safety. We now permit limited use of designated check airmen to conduct these checks on behalf of the agency, as they are used regularly to conduct checks for all other airlines.

8. Are you aware of any union efforts to harass or intimidate pilot candidates at Eastern? Have any of these efforts involved physical threats or intimidation?

ANSWER: EAL continues to report that pilot applicants and trainees continue to be harassed. We understand from Eastern that several people in both the pilot and mechanic ranks have received threats of physical harm.

9. Has the FAA received any reports of efforts by union pilots at other airlines to disrupt or harass Eastern's operations or to interfere with Eastern's pilots during the course of their flights? What safety impact do these actions have?

ANSWER: Since the strike began, the FAA has received several reports of attempted disruption or harassment of EAL operations and appropriate enforcement investigations have been initiated. EAL continues to report, and the FAA has confirmed, incidents of communications interference in the Northeast and Southern areas of the United States. Any form of harassment or intimidation of any flight crewmember while performing flight duties could have serious implications for safety, and may constitute a violation of 14 C.F.R. 91.8, as well as other laws. Our surveillance efforts have increased to detect these incidents and deter their recurrence. We are working with the Federal Communications Commission and the Department of Justice, including the Federal Bureau of Investigation, in several cases involving interference with communications on air traffic control frequencies.

10. Continental Air Lines is perhaps the best example of an airline that at one time had serious labor-management problems. Given that Frank Lorenzo is also the Chairman of Continental, would you comment on Continental's regulatory compliance posture?

ANSWER: While Continental did have significant compliance difficulties in the early to mid-80's, it currently meets all applicable safety regulatory requirements. In the spring of 1988, at the time of the FAA safety and OST fitness reviews of EAL and Texas Air, the FAA performed ramp inspections of all Continental Air Lines aircraft. No significant instance of non-compliance was found.

11. Recently, you pulled the certificate for Eastern's maintenance base at Kennedy Airport in New York. Was this the result of mismanagement by Eastern or foul-ups by its employees?

ANSWER: In May 1989, when confronted with FAA findings of systematic maintenance violations at Eastern's Kennedy Airport (JFK) maintenance facility, Eastern requested that its operations specifications be amended to delete its maintenance operation at JFK. The FAA investigation which led to these findings, which is ongoing, revealed that Eastern had repeatedly failed to follow its system for recording and inspecting maintenance performed so as to assure that aircraft approved for return to service are airworthy. Eastern surrendered its Kennedy Airport repair station certificate indefinitely. Because the investigation has not yet been completed, any further discussion would be inappropriate.

12. Eastern is in the process of hiring a large number of pilots. What are you doing to ensure that two inexperienced pilots are not paired together in the same cockpit?

ANSWER: Pilot assignments are made in accordance with EAL's approved procedures, which generally limit the pairing of less experienced crewmembers in accordance with the FAA's Air Carrier Operations Bulletin 8-88-1. This means that, ordinarily, at least one member of a crew pair will have at least 100 hours experience in the aircraft type or, if not, the captain must perform all of the takeoffs and landings; in the latter case, the related visibility (weather) minima are more restrictive as well. In some instances, where relatively inexperienced pilots are assigned to the same flight, this pairing must be approved by the Staff Vice President for Technical Systems and Safety. In terms of crew pairing, any company that has purchased new equipment, undergone expansion, or been faced with a strike may have to pair, for a short period of time, pilots who have relatively fewer hours of experience in a particular type of aircraft. All EAL pilots are required to meet the FAR requirements for minimum hours, certificates, and ratings to complete the required training program and flight checks. The term "inexperienced" can be misleading and often denotes only the relative number of hours on a route or in a type of aircraft.

We hope this information will be helpful.

Sincerely,

Greg S. Walden

Gregory S. Walden
Chief Counsel

cc: The Honorable James L. Oberstar

Mr. **Oberstar**. We have one final witness whom I do not know by face, Mr. Rolleston. Is Mr. Rolleston here?

Mr. **Rolleston**. I am here.

Mr. **Oberstar**. Please identify yourself.

TESTIMONY OF MORETON ROLLESTON, JR.

Mr. **Rolleston**. Thank you, Mr. Chairman. My name is Moreton Rolleston, Jr. I am from Atlanta, Georgia. I am an attorney and been practicing two years longer than Mr. Shapiro has incidentally. You know, it takes a bird dog to know another bird dog, and if I ever saw a man representing a client, I will tell you Mr. Shapiro is representing Eastern Air Lines. The only reason I have waited this 10 hours—this will take about 10 minutes I hope—was to try to inform at least the Chairman, even though nobody else is here, on some things that are absolutely incorrect that has been told this Committee today.

Mr. **Oberstar**. Please be seated.

Mr. **Rolleston**. If you do not mind, I will stand up, I am used to standing and talking, but I will sit down if you say so.

Mr. **Oberstar**. I just do not want you to feel uncomfortable.

Mr. **Rolleston**. I am comfortable standing, Your Honor. I have been standing practicing law a long time. Mr. Shapiro said that Mr. Lorenzo in Texas was entitled to money for his Texas Air stock in Eastern Air Lines. There is nothing in the law, the bankruptcy law, that says a debtor in possession is entitled to get paid for his stock. It is absolutely untrue. And when he made his three conditions, one of which was Mr. Lorenzo and his other people who own stock, were entitled to be paid out of the bankruptcy, there is no basis for it.

The second thing that this Committee has not been advised of, there is 120-day waiting period during which the debtor in bankruptcy can bring his plan in, but it is not mandatory. Judge Lifland is simply not doing anything about it. He could have cut it off after 30 days. The law provides for it. The law also provides that the judge under Bankruptcy Code 1104, write it down 1104, has the right to appoint a trustee whenever there is fraud or gross mismanagement. There is no allegation in this proceedings in the bankruptcy court about fraud. There is a 60-page affidavit from Mr. Kupersmith that is filed of record of which the gentleman from California is entitled to see, if he wants to of the things that Mr. Kupersmith and ALPA think have been improper, gross mismanagement.

Maybe you have not heard of them, but let me just give you one of them. Eastern Air Lines had one of the best reservation systems in the world. It ranks I think three in volume. It was owned by Eastern Air Lines. Eastern Air Lines was directed by Texas Air to sell it to Continental Airlines for $100 million. They sold it, but they did not get cash for it, they got a note at 6 percent interest due in 25 years. And then Continental turned around and charged Eastern Air Lines money to use the reservation system, sufficiently, I assert, to pay the note interest which was due on it. A seller and a purchaser controlled by one person.

Another little fact. Eastern Air Lines pays Continental Airlines some money for every gallon of kerosene that they burn. Why? Just two instances. If this Committee really wants to see what is being done, it is not any confidential capacity. Kupersmith's affidavit has been filed in court. I have read it. It is about 59 pages long, with about 60 pages of exhibits, and it itemizes item by item the things that could be considered mismanagement which could be used to appoint a trustee.

You know this is a sad day really because if we expect what is going to happen which Eastern Air Lines' advocate, Mr. Shapiro, pointed out to this Committee, there are a lot of four strippers back here who will never fly a commercial airline again. And I will tell you why. These people, these pilots who have not sought increase in pay are not going to fly for Eastern Air Lines under the present management or if it continues under Lorenzo. Right or wrong, that is the situation. The 3,000 other pilots that are not here today are not going to go fly for Eastern Air Lines.

And I will make a prediction which is a dangerous thing to do, unless something else happens Eastern Air Lines under the reorganization plan, run by Lorenzo will be broke and out of business in 60 days. Why? They have admitted that they are losing in cash, not in bookkeeping $1.7 a day. They have got in the bank right now, I am told as of yesterday, about $50 million. In two months time that money will be gone. Even Lorenzo will not have any money to run Eastern Air Lines.

But I did not come here just to talk. I came here to make a suggestion to this Committee. And I wish all the members of this Committee were here to listen to it and at least consider it. Because there is a way for Eastern Air Lines to start flying now, and for these 33,000 pilots and all the other 20,000 employees who represent 100,000 people whose families practically have no income now. They could go back to work. Eastern Air Lines as a full operating airline could go back to flying as soon as it could recondition the planes and re-certify the pilots, if you appoint a trustee.

Machinists, the pilots, the flight attendants have said they will not work for Eastern Air Lines under Lorenzo. But that they would work under a trustee. If a trustee was appointed by the court, that trustee could operate the airlines as long as it was possible financially until maybe somebody else would come along and buy it. There are other people. I know some other people who are not interested in buying Eastern Air Lines in the condition it is in now, because it is a run down airline and it is practically nonexistent.

Plus the fact that all of the bidding on Eastern Air Lines has been a published stun in the newspaper. A lot of people with money do not want to get any publicity competition. There are other people who would buy it probably from a trustee, if he were appointed. If a trustee was appointed, these people right here would go back to work tomorrow. I am telling you that these people would probably work for nothing for a month or two to get this airline started again. They have agreed to work for six months at reduced pay. What is their choice. Work for nothing and get the airline started or stay out without a job probably for the rest of their lives.

These gentlemen sitting in here with those stripes on cannot go to another airline. How could the captain of a ship drop down on another ship to a purser? How can he go from a captain, a man 55, in the late 50's, and take a job that is run by a 25 or 30 year old second officer? They are not going to do it. In the first place, they probably could not get a job, simply because they have got too much seniority.

So what I have got to suggest to you, Mr. Chairman, while all the talk was going on, I jotted down a small resolution that I would like to put in the record. And I ask you to make it available anyway and tell me at least that it is in the record, if anybody wants to read it.

Let me say one other thing. I am involved in a litigation. I filed a motion as a creditor and in the public interest is the way it is worded. And the judge set it down for a hearing 10 days after it was filed, and called me up and said it is set for a hearing, can you please come. I have been to three hearings and there has never been an order passed on that motion yet. It is still pending. It may come up on the 12th again.

I do not represent anybody. Nobody is paying me a dime. I am here on my own expense and I am almost missing my airplane back to Atlanta, but I may make it yet. But it is worth putting this in your record, please. Judge Lifland has twice, publicly, from the bench, said he thought that everybody who was interested in saying was represented except the public. That is why I got in it. He has invited you to make some move, some expression for the public. You and anybody else in the public. And so I do not think you would be infringing on his rights. I do not think you would embarrass him. I do not think this Committee by taking some action would do anything but help make the judge think.

Every person who talks to the judge and makes a presentation to him affects his judgment. And this Committee has got a right and I would say an obligation, since you have gone to all of this trouble to take a position and express it to the judge. I think he would appreciate it. He is a smart judge. I was listening to him, but he has, in my opinion, done all he could do in the bankruptcy law. I do not think the bankruptcy law is so archaic as it has been presented to you people. It is a working law.

My resolution: Whereas, Judge Lifland has indicated he would welcome some people supporting any public interest, and whereas the protection of the public interest in aviation matters is a responsibility of this Committee, and third, whereas the public interest requires that Eastern Air Lines resume full operation as soon as possible. And the last whereas, it appears that the pilots, the mechanics, the flight attendants will not go back to work for Eastern Air Lines under the present management, but will work for a trustee appointed by the court. And therefore, we do hereby adopt the following resolution. Resolved, that this Committee wishes to inform the United States Bankruptcy Court of the Southern District of New York that we have concluded that an immediate solution of Eastern Air Lines bankruptcy is for the court to appoint a trustee to operate Eastern Air Lines.

I think it is appropriate. I think the judge would appreciate it. I think it might help. Thank you, Your Honor.

Mr. OBERSTAR. Thank you very much, Mr. Rolleston. [Applause.]

I never saw or heard Clarence Darrow in action. He could not have been more eloquent or to the point. Yes, indeed, the CSR sale is scandalous. It is the modern day equivalent of treating the patient with lesions, and appointing a trustee certainly has been addressed by other witnesses. Had that step been taken, perhaps we might be closer to a resolution of the issue in keeping Eastern Air Lines operational as it was pre-strike.

Accepting the recommendation of this Committee in the legislation, we reported in which the House approved. Appointment of a Presidential Emergency Board would have breathed new life into Eastern. We have tried with the resources available to this Committee and within the law and separation of powers to do all that we can to bring about a good result. I think at each step our judgement has been right, our action has been right, it has been appropriate. We will continue to take whatever additional action may be appropriate, including appealing to the judge.

I might say that history was made today when the examiner testified at this hearing. I do not know of another case when that has occurred in any other bankruptcy proceeding. Bankruptcy is not an archaic law, as you said, but it is a law with some limitations. And some of those that can should be addressed in future legislation.

I wish at the conclusion of this hearing we had a resolution of the problem, something that we could implement, put into effect, restore the livelihood, some dreams and hopes and aspirations to the careers of those who have given so much of themselves to Eastern Air Lines, and to the public that they have served, in a great sense of public dedication. I wish there were an answer. If it were for this Chairman to put into effect, it would be done. But we do not operate that way in this system of checks and balances in our Government and separation of powers. So we must continue to use the instruments available.

We will propose changes in the bankruptcy law. We will continue to insist that the Federal Aviation Administration ride herd on the emerging Eastern Air Lines to keep it under a close rein. We will insist that the Department of Transportation use all the authority that it has to assure that these plans are viable, practical, and effective plans for operation. That the examiner and the bankruptcy judge not abandon the possibility of resurrecting Eastern. And that the Ritchie or any other group that may still be attempting to acquire Eastern and restore it, will give every full measure of consideration that is possible under the law and under the proceedings of bankruptcy.

We will do all that we can. I wish there were more that we could do. It is a shame that there is yet another step in that direction and in that spirit. And we thank all of you who sat through here through this hearing today so patiently. I know that your lives and the lives that are on the line, the well being of your families and I understand that. I come from a union family. We went through strikes, through deprivation, and through economic dislocation. I understand firsthand what it is like. That is why I have stayed here this day and many other days trying to bring about justice in the work place.

The Subcommittee stands adjourned.

[Whereupon, at 8:32 p.m., the Subcommittee adjourned, subject to the call of the Chair.]

ADDITIONS TO THE RECORD

PUBLIC WORKS AND TRANSPORTATION
SUBCOMMITTEE ON AVIATION

THE CURRENT CONDITION OF EASTERN AIR LINES AND THE PROSPECTS FOR ITS RESTORATION AS A MAJOR CARRIER.

HEARING DATE: THURSDAY, JUNE 29, 1989, 11:00 A.M.

STATEMENT BY:

CAPTAIN GARY F. KOSAK
2055 IXORA ROAD
NORTH MIAMI, FLORIDA 33181
(305) 891-9659

Eastern Air Lines was once one of the finest airlines in the aviation industry. As one of the pioneers of aviation, Capt. Eddie Rickenbacker, its founder, brought to our airline, a legac, and a perseverance that caused Eastern to be on the cutting edge of aviation development and growth.

In its 60-plus years of history, Eastern had grown from a small company of Pitcairn Mailwing bi-planes, to a fleet of as many as 289 jet aircraft, from a handful to as many as 42,000 employees. Truly, Eastern has been, and is a jewel in the American economy, and to quote Judge Burton Lifland of the U.S. Bankruptcy Court in New York, a "wasting asset".

As a pilot for Eastern Air Lines for more than 20 years, I have always been proud to be part of Eastern's team. Eastern has often been first in marketing, and in the introduction of new passenger aircraft. It was Eastern's people who developed and built the infamous "Eastern Shuttle", which tragically has been sold off. It was Eastern that first introduced the B-727 to the American public. It was Eastern that first flew the L-1011 in scheduled service, and it was Eastern that was first in the introduction of the recently developed B-757.

Miami, Atlanta, and other cities have developed into the thriving cities that they are today, largely because of the efforts of Eastern Air Lines employees. Well over one hundred cities were at one time served by this once proud airline.

In February of 1986, Eastern Air Lines was sold in the blackness of night. The atmosphere around the sale is still clouded with suspicion. Under the direction of Mr. Frank Borman and Eastern's board of directors, Mr. Frank Lorenzo of Texas Air Corporation, was paid an unrefundable $20,000,000 simply to make an offer on the airline. Eastern was sold. Mr. Lorenzo offered to indemnify the Eastern board of directors in the even that they were later sued for fiduciary irresponsibility. Salomon Brothers, which was hired by the Eastern board to appraise the terms of the sale refused to recommend them as "fair".

Eastern, which was the fifth-largest airline in the country was sold for roughly $640,000,000 or $10 per share. Only $388,000,000 of that price was paid in cash, and the rest was in junk bonds. Of that cash, Texas Air Corporation put up only $280,000,000 and **EASTERN AIR LINES PUT UP $108 MILLION OF ITS OWN CASH TO PAY FOR ITS OWN TAKEOVER!** As part of that same agreement, Frank Lorenzo would have 51% of the voting stock before the shareholders had a chance to vote on the acquisition, and before any competing bids could be made.

Once gaining control of Eastern, Mr. Lorenzo began to attack the employees. One of his many teams of lawyers immediately set out to file suit against Eastern's pilots, claiming that their current labor agreement was invalid. After months of litigation, the courts ruled in favor of Eastern's pilots. Mr. Lorenzo and his lawyers appealed. More months of litigation followed, and once again, the Eastern pilots were upheld in the appeals court. This was only one of several law suits filed by Mr. Lorenzo against his own employees. He is still suing us under the RICO act, a law designed to prosecute racketeers and extortionists.

There was a constant propaganda campaign in the company newspaper which spoke of "marketplace" wages, always inferring that Eastern's employees were paid too much. According to available statistics, on a per-employee basis, Eastern's employees were somewhere in the lower middle of the pack with regard to compensation among the major air carriers. The pilots were already 35% BELOW THE INDUSTRY **AVERAGE**, and Eastern pilots would have needed an approximate **50% RAISE** to match the industry standard set by Delta Air Lines.

The current strike by Eastern's machinists and honored by the pilots and flight attendants, is NOT over wages or benefits. It was a last-resort attempt to save our airline from further dismantling and destruction. It is this strike which has enabled me to communicate with this aviation subcommittee which hopefully will shine the laser light of truth on the Eastern story over the past three and a half years.

HUNDREDS OF MILLIONS OF DOLLARS began to disappear from Eastern in a variety of ways. A conservatively valued $350,000,000 computer reservations system (SODA) was "sold" to Texas Air Corporation by Eastern's new management for a $100,000,000 I.O.U. due in the year 2012. Since then, Eastern has had to pay Texas Air Corporation some $10,000,000 **PER MONTH** to use its own computer system.

Instead of purchasing its fuel from normal vendors, Eastern has been forced to buy from a Lorenzo-owned brokerage and is assessed a surcharge of 1 **cent per gallon** for every drop of fuel purchased. This surcharge has cost additional tens of millions of dollars per year from an already fragile Eastern.

Despite its need for cash, Eastern's new management lent already-bankrupt People Express Airlines $25,000,000. This same management lent Continental Air Lines $40,000,000 while at the same time applying to the Internal Revenue Service for waivers of pension plan payments.

Eastern loaned Continental Air Lines $11,000,000 to purchase 11 gates at Newark from itself for $1,000,000 per gate. The value of each gate at Newark at the time was over $8,000,000.

Eastern Air Lines pays Texas Air Corporation a $500,000 per month "management fee", despite the fact that Eastern has a full compliment of "managers".

And the list of transactions goes on and on, totalling more than ONE **BILLION DOLLARS** in cash and assets which were "upstreamed" from Eastern Air Lines to Frank Lorenzo's other holdings over three years.

Eastern's management arbitrarily cancelled thousands of pilot vacations. This pilot has not had a vacation in over two years, and had over 60 days of "banked" vacation and an entire months's paycheck lost because of this bankruptcy.

Very significant to this pilot, is the fact that I along with other employees have approached the senior management of Eastern Air Lines, and Frank Lorenzo himself with offers to help bring peace to Eastern. I personally offered to Frank Lorenzo (chairman of Texas Air), Phil Bakes (president of Eastern), and Tom Matthews (Vice-President of Labor Relations) the opportunity to work with one of the most able and best known labor/management peacemakers in the nation.

Mr. Wayne Alderson, a former candidate for Secretary of Labor, and a business consultant who has been able to bring reconciliation and peace to many an American business through his VALUE OF THE PERSON seminars, was turned down by Mr. Frank Lorenzo and Mr. Phil Bakes in his offer to bring reconciliation to Eastern's management and labor groups. Mr. Alderson's services were offered FREE of charge to Eastern Air Lines, however, it became more and more obvious that there was no desire on the part of this management to have peace. They seemed more interested in bludgeoning the employees into some perceived submission that would apparently open the door wider for the continued stripping of Eastern's assets.

A statement made by Vice-President of Labor Relations, Tom Matthews, when presented with the truth that he and Eastern's management were running Eastern over a cliff, was as follows: "Not only are we prepared to run Eastern over a cliff, but we (meaning the management) have parachutes and we have mattresses at the bottom". This hardly bespeaks a management with the best interests of Eastern at heart.

When asked by me as to why Eastern did not choose to work with Mr. Wayne Alderson to bring about labor/management peace, Mr. Matthews stated to the effect, "we didn't need that kind of help. We know what we're doing. This is an economic problem".

Today, only 6 years after the same tactics were used at Continental Air Lines, the same man, Frank Lorenzo, has plunged yet another American air carrier into bankruptcy, and is now trying to proceed with an apparent two-step liquidation under the guise of a chapter 11 proceeding.

While Mr. Lorenzo and his lawyers have been working laboriously to disassemble and devour Eastern, another man has come upon the scene and wants to buy, operate and grow Eastern, thus preserving more choice for the American traveling public, maintaining jobs for tens of thousands of Eastern's employees, and preserving the economies of several American cities served by Eastern. Mr. Joseph Ritchie has the full support of the vast majority of Eastern's employees and should be supported by this Aviation Subcommittee in rescuing Eastern Air Lines from the grips of incompetent and immoral business practices.

I am of the strong opinion that the founders of our country and even the more current legislators who authored airline deregulation did not have as their vision, the Frank Lorenzo flavor of free enterprise. I believe that I have the agreement of the vast majority of American people, including businessmen and legislators, that if business methods such as those practiced by Frank Lorenzo, are allowed to proliferate, that we will see the demise of American business, and thus our economy.

To add to this, the air transportation system in this nation cannot be treated as shoe stores or hamburger stands to be bought and sold for the sake of personal gain, and at the expense of stability, safety, and the employment of thousands of Americans. There must be as least a minimum of government protection against this inane practice of the corporate raid, resultant leveraged buyouts, and certainly the incredible abuse of the nation's bankruptcy laws as yet another tool in the corporate raider's burglar bag.

I am pleading with this committee and hoping that I am facing statesmen and not politicians. You, gentlemen, have the power to put a stop to this perversion of the American way. It is my earnest hope and prayer, that you will take the high road of protecting the American public, and the thousands of Eastern employees by saying "NO" to Frank Lorenzo, his business practices, and his intolerable manipulation of our nation's bankruptcy laws.

I am indebted to this committee for the opportunity to communicate with you.

Respectfully yours,

Gary F Kosak

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